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LEGAL-PROCESS CONSTRAINTS ON THE REGULATION OF LAWYERS' CONTINGENT FEE CONTRACTS

Ted Schneyer*

INTRODUCTION

Unlike their counterparts in other countries¹ and certain other professions,² lawyers in the United States have long been permitted to charge contingent fees. With lawyers now representing plaintiffs on a contingent fee basis in most of the roughly one million tort cases that are filed each year,³ the practice is more common than ever. Yet it has always been controversial. Early in the century, when the American Bar Association ("ABA") drafted its first ethics code for lawyers, the propriety of contingent fees was hotly debated.⁴ As adopted in

* Milton O. Riepe Professor of Law, University of Arizona College of Law. Thanks to Judith Resnik for comments on an earlier version of this Article, which was presented at the Third Annual Clifford Seminar on Tort Law and Policy, addressing Contingency Fee Financing of Litigation in America, Chicago, Illinois, April 4-5, 1997.

1. Contingent fees have long been prohibited, for example, in England and Scotland. For recent steps relaxing the bans in those countries, see Richard W. Painter, *Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty*, 71 CHI.-KENT L. REV. 625, 627 n.10 (1995).

2. Professional associations in medicine and accounting still regard the use of contingent fees in those occupations as unethical, but their positions are increasingly being challenged by doctors and accountants. For example, some medical clinics specializing in assisted reproduction have begun to offer in vitro fertilization services on a contingent fee basis; if no pregnancy or delivery results, some or all of the fee is returned. An American Medical Association ("AMA") task force recently condemned this practice as unethical on the authority of a 1977 AMA ethics opinion declaring it improper for physicians to charge contingent fees. See AMERICAN MEDICAL ASSOCIATION COUNCIL ON ETHICAL AND JUDICIAL AFFAIRS AND COUNCIL ON SCIENTIFIC AFFAIRS, ISSUES OF ETHICAL CONDUCT IN ASSISTED REPRODUCTIVE TECHNOLOGY 5 (1996) (on file with the *DePaul Law Review*). For developments in accounting, see Lester Brickman, *Contingent Fees Without Contingencies: Hamlet Without the Prince of Denmark?*, 37 UCLA L. REV. 29, 39 n.41 (1989).

3. For the data and calculations that support this estimate of annual tort filings, see Lester Brickman, *Contingency Fee Abuses, Ethical Mandates, and the Disciplinary System: The Case Against Case-by-Case Enforcement*, 53 WASH. & LEE L. REV. 1339, 1349 & n.45 (1996). Plaintiffs' lawyers take roughly 95% of all personal injury cases on a contingency. Painter, *supra* note 1, at 626 n.3 (citing sources).

4. Indeed, the contingency fee was the only hotly debated topic. EDSON SUNDERLAND, HISTORY OF THE AMERICAN BAR ASSOCIATION AND ITS WORK 111 (1953); see also ABA Committee on a Code of Professional Ethics, *Final Report*, 33 A.B.A. REP. 567, 570-71 (1908) (summarizing the debate).

1908, the ABA Canons of Professional Ethics reflected an uneasy compromise between prohibition and laissez faire. Canon 13 provided that contingent fees, where permitted by law, should be "under the supervision of the court"⁵—i.e., regulated—and not governed solely by market forces and general principles of contract law. This uneasy compromise still prevails. Every state permits lawyers to charge contingent fees⁶ except in the fields of criminal defense,⁷ divorce,⁸ and lobbying,⁹ where the arrangement is thought to raise special problems. But lawyers' contingent fee contracts are now subject to various forms of regulation, such as fee caps, from which other legal-fee agreements are spared.¹⁰ Still other forms of contingent fee regulation have recently been proposed.¹¹

Over the years, critics have tried to link contingent fees with a variety of evils, but today's critics focus on the charge that contingent fee contracts produce windfalls for lawyers, i.e. fees greater than necessary to induce lawyers to accept meritorious cases and pursue them competently. They claim that the excessive fee problem has become pervasive in the personal injury field and, therefore, justifies their proposals for more powerful or extensive regulation.¹² Other experts re-

5. CANONS OF PROFESSIONAL ETHICS Canon 13 (1908).

6. Maine was a holdout until 1965, when the state legislature finally repealed its ban on lawyers' contingent fees. CHARLES W. WOLFRAM, *MODERN LEGAL ETHICS* 527 & n.14 (student ed. 1986).

7. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(d)(2) (1994) (codifying the traditional ban on contingent fees in criminal defense cases). For assessment of the costs and benefits of the ban, and an argument that the ban should be relaxed, see generally Pamela S. Karlan, *Contingent Fees and Criminal Cases*, 93 COLUM. L. REV. 595 (1993).

8. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(d)(1) (1994) (banning "any fee in a domestic relation matter, the payment or amount of which is contingent upon the securing of a divorce or upon the amount of alimony or support, or property settlement in lieu thereof").

9. WOLFRAM, *supra* note 6, at 542 & nn.17, 19 (citing cases).

10. See *infra* notes 42, 85-87 and accompanying text.

11. See *infra* notes 42-46, 161-71 and accompanying text (discussing the Manhattan Institute's "early offer" proposal).

12. See, e.g., Brickman, *supra* note 2, at 105-11 (inferring that contingent fees regularly yield greater than competitive rates of return from evidence that most lawyers charge the same contingent fees to all their clients despite case-to-case variations in the odds of recovery and also from evidence that recovery rates and amounts increased over a 25 year period). Brickman and others have estimated that "no less than \$7.5 to \$10 billion in unethical, windfall contingency fees are now charged annually." Lester Brickman, *ABA Regulation of Contingency Fees: Money Talks, Ethics Walks*, 65 FORDHAM L. REV. 247, 314 app. A (1996) [hereinafter Brickman, *ABA Regulation*]. Brickman and two co-authors use such evidence to support their own complex proposal for a new form of contingent fee regulation. See LESTER BRICKMAN ET AL., *RETHINKING CONTINGENCY FEES* (1994) [hereinafter BRICKMAN ET AL.]. But see James A. Henderson & Theodore Eisenberg, *The Quiet Revolution in Products Liability: An Empirical Study of Legal Charge*, 37 UCLA L. REV. 479, 523 (reporting results of a relatively recent study showing a decline in plaintiffs' success rates in products liability cases); Charles Silver, *Control Fees? No, Let the Free Market Do Its Job*, NAT'L L.J. Apr. 18, 1994, at A17 (arguing that common use of

spond that, although lawyers might occasionally reap contingent fee windfalls, tighter controls are unnecessary because today's legal services market is competitive enough to keep excessive fees to a minimum.¹³ To the extent that debates on contingent fee regulation continue to focus on the magnitude of the excessive fee problem, they may never be resolved, because no consensus exists as to how to determine whether a particular contingent fee is excessive, let alone whether excessive fees are pervasive.

Perhaps scholars can better advance the debate by paying closer attention to the institutional capacities of courts, disciplinary agencies, and other enforcers to implement effectively, and at acceptable cost, many of the existing and proposed controls on fee amounts. Regulatory intervention is not justified in every instance in which consumer ignorance, third-party effects, or lack of competition produce market imperfections. Because regulatory cures can be worse than unregulated diseases, evidence of contingent fee abuse cannot, by itself, justify intervention. One must also show that a regulatory scheme combats the abuse effectively and at acceptable cost, including the cost to the legal system of administering the scheme. Accordingly, this Article tries to advance the debate on contingent fee regulation by focusing not on the magnitude of contingent fee abuse (which I will assume to be more than negligible), but rather on the institutional limitations that can make well intended regulatory responses impractical, ineffective, or too costly to administer.

In other words, this Article treats the issues of how and how extensively to regulate contingent fee contracts primarily as a legal-process

standard contingent fees does not imply lack of competition, given the difficulty of estimating ex ante the odds that a particular case will succeed and the time it will require). Notice that even if all the personal injury lawyers in a community charge their clients the same percentage contingent fee, they might still compete for cases on the basis of reputation, with stronger cases gravitating to those who appear to get better results. Moreover, it is not necessarily the case that lawyers' profits increase when percentage contingent fees remain constant while recovery rates and average recoveries increase. The effort and skill lawyers put into producing recoveries and, therefore, lawyers' costs, may have increased as well.

13. See STUART SPEISER, *LAWUIT* 571 (1980) (asserting that contingent fees were higher in the past, with 50% being the typical rate before 1950); Marc Galanter, *Anyone Can Fall Down a Manhole: The Contingency Fee and Its Discontents*, 47 DEPAUL L. REV. 457, 457-458 (1998) (arguing that falling contingent fees are what we might expect from the demise of minimum fee schedules and bans on lawyer advertising in the 1970s, and from the gradual increase in the sophistication of clients, which all promote price competition); HERBERT M. KRITZER, *RHETORIC AND REALITY . . . USES AND ABUSES . . . CONTINGENCIES AND CERTAINTIES: THE POLITICAL ECONOMY OF THE AMERICAN CONTINGENT FEE* 16-28 (University Of Wis. Inst. for Legal Studies, Dispute Processing Research Program Working Paper No. 11-8, 1995) (finding that the incomes and hourly returns of contingent fee and other lawyers are very similar and inferring that plaintiffs' personal injury work is no less competitive than other legal fields).

issue, whose proper resolution depends on appreciating the limited capacities of the institutions that create and enforce regulatory measures. I distinguish among four different problems that critics have associated with lawyers' contingent fee contracts and I assess, from a legal-process standpoint, the existing or proposed regulatory responses to each problem.¹⁴ In this way, I hope to show that cost-justified regulatory techniques have been devised in response to some concerns, but that enforcement difficulties make the value of most responses to the excessive fee problem doubtful.

The Article proceeds as follows: Part I defines contingent fees and identifies their distinctive functions.¹⁵ It also discusses recent developments in contingent fee practice which may have implications for future regulation. Part II focuses on three relatively manageable concerns that have been raised over the years about lawyers' contingent fee contracts: client confusion about the mechanics of computing contingent fees, the opportunistic use of contingent fee contracts to discourage clients from changing counsel, and perverse effects on lawyers' incentives in selecting and handling cases.¹⁶ Part II links various regulatory measures to each concern and explains why these measures are generally unobjectionable on administrative or legal-process grounds. Part III looks at regulatory responses to the allegedly pervasive problem of excessive contingent fees.¹⁷ It argues that, unlike the measures discussed in Part II, the existing or proposed responses to this concern cannot be effectively administered at acceptable cost. Some overestimate the enforcement capacity of courts and disciplinary bodies, while others rely on overly crude devices to skirt those enforcers' limitations.

I. BASIC FUNCTIONS AND EVOLVING USE OF THE CONTINGENT FEE

Private lawyers and their clients use a variety of fee arrangements, including contingent fees, hourly rates, and flat fees.¹⁸ Part I distinguishes contingent fees from others, explains why many clients find contingent fees attractive, sketches two recent developments in contingent fee practice, and speculates briefly about their implications for future regulation.

14. See *infra* notes 18-108 and accompanying text.

15. See *infra* notes 18-54 and accompanying text.

16. See *infra* notes 55-101 and accompanying text.

17. See *infra* notes 102-78 and accompanying text.

18. WOLFRAM, *supra* note 6, at 504.

A. Contingent Fees Defined

Unlike conventional hourly fees or flat rates, lawyers become entitled to a contingent fee only if they obtain a given result for their clients. When lawyers are retained to help clients recover compensation for personal injuries, and agree to be paid only if there is a recovery, they are working on a contingency. Their fees, if earned, might be a flat sum or the product of the hours invested in the case and an agreed-upon hourly rate. Usually, however, they are a percentage of the amount recovered. A percentage contingent fee may be "unitary," or may vary with the stage at which the matter is resolved (e.g., one-third of the recovery if the case settles before trial; forty percent thereafter).¹⁹ Contingent fee terms usually are set in a retainer agreement when representation begins. But a claim for legal fees for achieving a certain result can also arise by operation of law, such as when a court awards fees to lawyers who generate a common fund for their clients in "aggregate litigation,"²⁰ or to lawyers whose clients prevail in cases governed by a fee-shifting statute.²¹

B. The Functions of Contingent Fees

A client might choose a contingent fee arrangement for any of four reasons, which I shall call the contingent fee's access, credit, anti-

19. See Bruce L. Hay, *Optimal Contingent Fees in a World of Settlement*, 26 J. LEGAL STUD. 259, 263-65, 270 (1997) (distinguishing unitary from bifurcated percentage contingent fees, which involve different rates depending on whether a case settles before trial, and arguing that the more beneficial method for the client generally is the bifurcated percentage fee plan, except in certain cases in which the client exercises real control over settlement decisions, in which cases the two methods should produce the same results).

20. "Aggregate litigation" includes class actions as well as individual cases that are consolidated by court order and then managed by the lawyers the presiding judge appoints to a Plaintiffs' Steering Committee. Judith Resnik et al., *Individuals Within the Aggregate: Relationships, Representation, and Fees*, 71 N.Y.U. L. REV. 296, 299-300, 314 (1996) [hereinafter Resnik et al.]. Whenever a proposed class action settlement calls for fee payments, the court must approve the fee amount along with other aspects of the settlement. *Id.* at 337; see FED. R. CIV. P. 23(e). In common fund cases, the federal courts award fees under the equitable "common fund" doctrine, Resnik et al., *supra*, at 337-38, and set the fees either on the basis of what the court considers an appropriate percentage of the fund created, or under the "lodestar method," which requires the judge to determine the number of hours counsel reasonably spent on the case as well as an appropriate hourly rate, and then to multiply these sums to arrive at the fee. *Id.* Many courts prefer the percentage-of-fund method, which may be easier for trial judges to administer and harder for appellate courts to second-guess. *Id.* at 340.

21. See, e.g., 42 U.S.C. § 1988 (1994) (providing for fee shifting in federal civil rights cases). Where a prevailing party is entitled to attorneys' fees from the opposing party under this or other federal fee-shifting statutes, the Supreme Court requires the award to be calculated by the lodestar method, rather than as a percentage of the client's recovery. *City of Burlington v. Dague*, 505 U.S. 557, 562-67 (1992); *Blum v. Stenson*, 465 U.S. 886, 895 (1984).

shirking, and insurance functions.²² Together, these functions are valuable enough to make a ban on all contingent fees unthinkable, despite the dangers associated with them.²³ Above all, contingent fees promote access to legal services. Clients often find it impossible or imprudent to hire a lawyer on any other basis. If contingent fees were banned, many deserving clients could not effectively pursue legal redress for their injuries. This would be more than a personal hardship or injustice. It would weaken the state's power to deter wrongful conduct through liability rules instead of administrative rules and penal statutes. The efficacy of liability rules depends on private enforcement.

The contingent fee expands access to legal services for those who are so averse to investing in a potentially fruitless lawsuit that they would not retain a lawyer on any other basis. More importantly, it expands access for those whose only substantial asset is the very claim they need a lawyer's help to pursue. Typically, such claims cannot be assigned to other parties who might be better situated to hire a lawyer on a non-contingent basis.²⁴ Nor can claims serve as collateral for loans that would enable claim holders to hire a lawyer on a non-contingent basis.²⁵ As a practical matter, one can only use an unliqui-

22. These functions have long been recognized. For an early summary, see Murray L. Schwartz & Daniel J.B. Mitchell, *An Economic Analysis of the Contingent Fee in Personal-Injury Litigation*, 22 STAN. L. REV. 1125, 1125 (1970) [hereinafter Schwartz & Mitchell].

23. Even its sharpest critics concede that the contingent fee is vital to the vindication of important legal rights. See BRICKMAN ET AL., *supra* note 12, at 13. For a discussion of how a ban on contingent fees might affect the American legal system, see generally Samuel R. Gross, *We Could Pass a Law . . . What Might Happen if Contingent Legal Fees Were Banned*, 47 DEPAUL L. REV. 321 (1998).

24. State law prohibits the purchase or sale of personal injury claims that have not been reduced to judgment. See, e.g., *Sprung v. Jaffe*, 147 N.E.2d 6, 8-9 (N.Y. 1957); N.Y. JUD. LAW §§ 488, 489 (McKinney 1983). Even if the sale of such claims were permitted, one might not expect a robust market to develop because assignees might find it hard to ensure that assignors would cooperate in prosecuting the cases once they had sold their interest.

25. E.g., *McKellips v. Mackintosh*, 475 N.W.2d 926, 929 (S.D. 1991) (voiding as against public policy an agreement whereby a bank official would lend litigants money to pursue a trademark infringement suit in exchange for a portion of the potential award or settlement); see also Schwartz & Mitchell, *supra* note 22, at 1125 (pointing out that personal injury clients rarely have access to capital markets to borrow funds against the prospect of a recovery in litigation). Once a claim is reduced to judgment, however, the plaintiff can assign a portion of the judgment in return for funds needed to defend the judgment on appeal. A lawyer-owned company in California has begun to offer cash to plaintiffs whose judgments are on appeal, in return for a share in the judgments if they are upheld. The company will not take a majority interest in any judgment, or control the conduct of the appeal. Painter, *supra* note 1, at 633. Professor Painter defends this innovation and, more generally, argues that relaxing the ban on assigning tort claims could reduce contingent fees by enabling non-lawyers to compete with lawyers in selling tort plaintiffs financial credit and legal-expense "insurance." *Id.* at 677-87.

dated tort claim to finance legal services by finding a lawyer who will invest in that claim by taking the case on a contingent fee.²⁶

Second, even clients who could pay lawyers on another basis may be attracted to contingent fees as a source of financial credit.²⁷ Unlike lawyers who charge hourly rates and bill periodically, or charge flat rates and expect at least some payment before work is completed, the contingent fee lawyer is not paid until the client's matter is resolved. Meanwhile, the client retains the funds that would otherwise have been paid out in fees.

Third, clients who find it hard to monitor or evaluate legal work use contingent fees to discourage their lawyers from "shirking."²⁸ Shirking often takes the form of pursuing a client's case with less effort and care than lawyers would exert on their own behalf or, put differently, less than reasonable lawyers would exert in order to maximize the client's net recovery.²⁹ Percentage contingent fees can also discourage shirking in the form of "running the meter"—devoting more time to a case than is cost-justified, as hourly-rate lawyers may be tempted to do.³⁰ Unlike business clients with recurring legal needs, many contingent fee clients are in no position to discourage shirking by holding out the prospect of future employment if the lawyer's current work proves satisfactory. Unable to motivate lawyers in that way, one-shot clients are understandably attracted to contingent fees, which help them align lawyer incentives with client interests by giving lawyers a piece of the action.

Finally, contingent fees offer clients a form of legal expense insurance.³¹ Lawyers who use contingent fees at all are apt to use them frequently. They share with each contingent fee client some of the risk that the client will end up with a negative return on his or her investment in the case. For sharing these risks, the lawyers factor into their fee a premium above the fees they would expect if they worked on a non-contingent basis. In effect, premiums collected from those whose cases succeed compensate lawyers for work on cases that fail.

26. Schwartz & Mitchell, *supra* note 22, at 1125.

27. *Id.*

28. Hay, *supra* note 19, at 259.

29. *Id.*; Bruce L. Hay, *Contingent Fees and Agency Costs*, 25 J. LEGAL STUD. 503, 503-04 (1996).

30. On the other hand, although percentage contingent fees give a lawyer and her client a common economic interest in victory, they may motivate the lawyer to devote fewer hours to the case than might be expected to maximize the client's net recovery, because the lawyer is not compensated directly for her time. Kevin M. Clermont & John D. Currihan, *Improving on the Contingent Fee*, 63 CORNELL L. REV. 529, 536 (1978) [hereinafter Clermont & Currihan].

31. Schwartz & Mitchell, *supra* note 22, at 1150.

Premiums can be attractively priced from the client's standpoint because the lawyers not only share risk but diversify it. By taking a portfolio of cases, lawyers assure themselves of relatively predictable earning streams, even if they are not much better than their clients at divining which cases will fail, succeed modestly, or yield large recoveries.

C. The Changing Nature of Contingent Fee Practice: Potential Regulatory Implications

The techniques for regulating contingent fees which will be analyzed in Parts II and III have all been designed with classic contingent fee clients in mind—individual plaintiffs who contract with lawyers for representation in personal injury cases.³² Such clients are often unaccustomed to dealing with lawyers. They may be physically or mentally impaired by their injuries and, therefore, in no position to shop around for a lawyer. Unless they belong to a legal services plan, they rarely have agents to help them negotiate fee contracts.³³ They are, in short, attractive candidates for regulatory protection. Yet contingent fee practice is moving away from the classic model in two respects that are beginning to complicate the regulatory environment. Before discussing the regulatory techniques that are in use or actively debated today, I want to briefly identify these trends and consider their implications for regulatory policy and politics in the future.

32. See Brickman, *supra* note 2, at 39 (referring to contingent fee's "traditional role" in personal injury cases).

33. Professor Brickman cites the lack of brokerage services to help personal injury victims seek out competent lawyers on favorable contingent fee terms as evidence that the market for personal injury work is uncompetitive. Brickman, *supra* note 2, at 107-08. Yet some legal services plans provide their members with precisely these benefits. See Wayne Moore & Monica Kolasa, *AARP's Legal Services Network: Expanding Legal Services to the Middle Class*, 32 WAKE FOREST L. REV. 503, 535-36 & n.181, 539-41, 543 (1997) (reporting that the American Association of Retired Persons ("AARP") has recently set up a multi-state legal services network for the benefit of its members, that participating lawyers must meet competence criteria, that those lawyers must agree to give AARP members a 20% discount on their normal fees—including contingent fees, that only bifurcated contingent fees may be used, and that the plan includes a system for responding to members' complaints about participating lawyers). Quite apart from legal service plans, more lawyers may become informal brokers for contingent fee cases, thanks to recent liberalization of the rules governing fee-splitting between unaffiliated lawyers. Compare MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(e)(1) (1994) (referring and receiving lawyer may share a fee if the division is in proportion to services provided by each or, with client's written consent, whenever the lawyers assume "joint responsibility" for the representation, even if receiving lawyer does all or most of the work) with MODEL RULES OF PROFESSIONAL RESPONSIBILITY DR 2-107(A)(2) (1980) (stating that the older code permitted fee splitting only in proportion to "the services performed and responsibility assumed" by each lawyer).

First, the domain of contingent fee practice is expanding to include many sophisticated clients. Businesses increasingly retain lawyers on a contingent fee rather than an hourly basis, and not just when they are cast in a plaintiff's role. Some businesses retain lawyers partly or wholly on a contingency basis in order to negotiate mergers or other transactions. Under this arrangement, the terms are no deal, no fee, or a reduced fee.³⁴ Some also retain counsel on a contingency basis to defend them in civil suits.³⁵ For example, if P sues D Corporation on a product liability claim, D might agree to pay its defense counsel an hourly fee plus ten percent of the difference between its estimated exposure and any lesser sum it ultimately pays the plaintiff. The contingent fee is a share of whatever liability the client avoids through the lawyer's efforts.

Business clients, especially those large enough to have in-house lawyers who help them negotiate fee agreements with outside counsel, do not need and presumably would not welcome fee caps or other regulatory protections designed with personal injury plaintiffs in mind. Recognizing this, the courts have never used ethics code restrictions or other extra-contractual law to protect corporate clients in contingent fee disputes with their lawyers, even where a contractual fee seems extravagant when measured against the work performed.³⁶ Accordingly, one implication of the contingent fee's expansion into corporate practice seems clear. To avoid wasteful oversight of private fee agreements, as well as unnecessary restraints on freedom of contract, lawmakers must expressly limit contingent fee regulation to fields where the rationales for regulation apply, as they normally do not in corporate practice. This tailoring of contingent fee regulation has ac-

34. Daniel Hertzberg & James B. Stewart, *Contingency Legal Fee for Merger Breaks Ground*, WALL ST. J., Oct. 24, 1986, at 31.

35. See, e.g., Michael Orey, *Good News, Bad News*, AM. LAW., July/Aug. 1991, Supp. at 6, 57-58 (reporting that Electronic Data Systems, a large corporation, now uses "defense contingent fees," which pay counsel a premium if less than a specified amount is recovered in litigation against the company, but require a fee discount if the amount is exceeded); see generally Comment, *Toward a Valid Defense Contingent Fee Contract: A Comparative Analysis*, 67 IOWA L. REV. 373 (1982) (discussing legality of defense contingent fees).

36. See, e.g., *Brobeck, Phleger & Harrison v. Telex Corp.*, 602 F.2d 866, 875 (9th Cir. 1979) (affirming a decision to enforce a contingent fee contract, negotiated with the help of the corporate client's in-house lawyers, that entitled the law firm to \$1,000,000 simply for preparing a brief in support of the client's petition for a writ of certiorari in an antitrust suit, where the petition was quickly mooted by a settlement that triggered the fee). Occasionally, ethics code restrictions on contingent fees, such as rules requiring contingent fee agreements to be in writing, expressly exempt fee agreements with business clients. See, e.g., ILLINOIS RULES OF PROFESSIONAL CONDUCT Rule 1.5(e) (1996) (excluding contingent fee agreements for the collection of commercial accounts or of insurance company subrogation claims from the formal requirements imposed on other contingent fees).

tually been underway for some time.³⁷ Older forms of regulation, such as ethics rules prohibiting lawyers from charging "excessive" or "unreasonable" legal fees,³⁸ are not limited to specific practice fields or even to contingent fees. By contrast, the newer regulations or proposed regulations, such as fee caps, only purport to govern the contingent fees that are earned in tort,³⁹ personal injury,⁴⁰ or medical malpractice cases.⁴¹

It is hard to gauge how the growing use of contingent fees in corporate practice will affect professional politics as it bears on contingent fee regulation. Business lawyers will presumably oppose regulatory measures that impinge on their own contingent fees. The deeper question is whether they will join personal injury lawyers in opposing regulatory initiatives aimed at those lawyers. So far, internal bar documents provide conflicting evidence on the point. Addressing a recent meeting of the ABA Torts and Insurance Section, one prominent litigator who represents corporate plaintiffs on a contingent fee basis defended the Manhattan Institute's controversial "early-offer" proposal,⁴² which plaintiffs' personal injury lawyers predictably oppose. That proposal would bar personal injury lawyers from charging their standard contingent fee on the portion of any ultimate recovery which

37. For example, some states have long imposed contingent fees in worker's compensation cases. See *Thatcher v. Industrial Comm'n*, 207 P.2d 178, 184 (Utah 1949). From its inception, the Federal Torts Claims Act has limited contingent fees to 25% of a recovery. 28 U.S.C. § 2678 (1993).

38. See MODEL RULES OF PROFESSIONAL RESPONSIBILITY DR 2-106(A) (1980) (barring lawyers from charging any "clearly excessive" legal fee, contingent or not).

39. See, e.g., FLORIDA RULES OF PROFESSIONAL CONDUCT Rule 4-1.5(f)(4) & cmt. (West 1997) (imposing presumptive fee-caps on contingent fees, depending on the amount and timing of a recovery, but noting that the caps do not apply to claims "arising in the commercial litigation context"); ILLINOIS RULES OF PROFESSIONAL CONDUCT Rule 1.5(e) (noting that the formal requirements specified for contingent fee contracts in Rule 1.5 do not apply to collection work or insurance subrogation claims); N.Y. R. OF CT. § 691.20(e) (McKinney 1997) (setting presumptive limits on attorneys' fees in tort cases and making a violation of these rules a disciplinable offense).

40. See, e.g., BRICKMAN ET AL., *supra* note 12, at 27-28, 69-82 (proposing that lawyers handling personal injury claims be barred from charging conventional contingent fees against that portion of any amount ultimately recovered which the defendant had offered as a settlement before or within 60 days after the lawyer was retained, even if the plaintiff rejected those "early offers" and the defendant took them off the table). The proposal, endorsed by the Manhattan Institute, a public policy research organization, is discussed *infra* at text accompanying notes 42-44, 171. A version of the proposal appeared as Proposition 202 on the California ballot in March 1996, but was narrowly defeated. Dan Bernstein, *More Legal Reform Votes*, SACRAMENTO BEE, Mar. 28, 1996, at A16 available in LEXIS, News Library, Papers File. Some aspects of the proposal also found their way into the Common Sense Product Liability Reform Act that President Clinton vetoed on May 2, 1996. Angel Wennihan, *Let's Put the Contingency Back in the Contingent Fee*, 49 SMU L. REV. 1639, 1670-72 (1996).

41. Brickman, *supra* note 2, at 125 & n.375 (citing statutes).

42. See *supra* note 40.

the defendant had offered in settlement proposals before or shortly after the lawyer was retained. The litigator pointed out that the proposal would simply give personal injury clients the same protections that sophisticated clients insist upon in negotiating their contingent fee agreements.⁴³ On the other hand, in a recent opinion,⁴⁴ the ABA Committee on Ethics and Professional Responsibility ("CEPR") refused to declare flatly unethical the common practice among personal injury lawyers of charging standard contingent fees (e.g., one-third of any recovery) rather than basing each fee on a customized estimate of the odds of gaining a recovery, the likely amount of the recovery, and the effort the case is likely to require. CEPR defended its position by observing that contingent fees are now common in corporate practice and other fields besides plaintiffs' personal injury work.⁴⁵ However, because *standard* contingent fees remain uncommon outside the personal injury field, at least in corporate practice, CEPR's observation was arguably irrelevant to the issue at hand. Why, then, did CEPR bother to make the point? One critic speculates that CEPR's observation was politically motivated—a gratuitous effort to mobilize lawyers of every stripe to "circle the wagons" and oppose new regulatory constraints on contingent fees in the personal injury field because "we are all contingency fee lawyers" now.⁴⁶

Contingent fee practice is also changing within the personal injury domain. With the sharp growth of aggregate litigation to deal with mass tort claims,⁴⁷ more plaintiffs' lawyers find themselves working primarily for contingent fees that are awarded *ex post* by judges, not negotiated *ex ante* with clients.⁴⁸ When individual tort claims are consolidated or turned into class actions, placed in the hands of court-appointed steering committees or lead counsel, and then brought to a

43. I do a lot of contingent fee work for large corporate plaintiffs and during our fee negotiations, little is left on the table. Often my clients insist on a fee structure not so different from [the early offer proposal]. So what's so awful with [an early offer] rule that assures clients without cloud of the same protection against a lawyer windfall.

Stephen D. Sussman, A Case for a Cease Fire, Address at the Annual Meeting of the TIPS Section of the ABA 8 (Apr. 15, 1994), *quoted in* Brickman, *ABA Regulation*, *supra* note 12, at 333 app. B.

44. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 94-389 (1994).

45. *Id.* (listing a broad array of non-traditional uses of lawyers' contingent fees).

46. Brickman, *ABA Regulation*, *supra* note 12, at 259.

47. *See, e.g.*, Resnik et al., *supra* note 20, at 298-300 (discussing the rapid evolution of aggregate tort litigation).

48. However, at least one federal court has experimented with setting contingent fees for plaintiff class action lawyers *ex ante*, by conducting an auction for the right to serve as lead counsel. *See In re Oracle Sec. Litig.*, 131 F.R.D. 688, 697 (N.D. Cal. 1990); *In re Oracle Sec. Litig.*, 132 F.R.D. 538, 542-48 (N.D. Cal. 1990) (awarding lead counsel rights based on bids for fees and costs constituting a percentage of the potential recovery in a securities class action).

successful conclusion, the judge determines what portion of the recovery to award the plaintiffs' lawyers as fees.⁴⁹ By contrast, when a traditional tort case yields a recovery, the trial court neither sets the fee, nor reviews the reasonableness of the contractual contingent fee. The only exceptions occur under special mandates,⁵⁰ when the client is a minor or an incompetent and thus a ward of the court,⁵¹ or (very occasionally) under the trial court's inherent authority to supervise lawyers appearing before it.⁵² Because it is unclear how the regulation of contingent fee contracts might affect judicial fee setting in aggregate tort litigation, one cannot predict whether the new breed of aggregate litigation specialists will favor or oppose measures that regulate those contracts. Since aggregate litigation specialists' fees are set by judges, these specialists might support caps or other constraints on contractual contingent fees, if only because they must share their fee awards with the lawyers who originally contracted to represent the individuals whose claims were later aggregated.⁵³ On the other hand, judges presiding over aggregate litigation sometimes use the percentage fees specified in those initial retainer agreements as their measure of the appropriate total fee award.⁵⁴ With this approach, if contract

49. See *supra* note 20.

50. For example, the Arizona Supreme Court requires trial judges in all medical malpractice cases to review the reasonableness of attorneys' fees in light of the general criteria set forth in Rule 1.5 of the Rules of Professional Conduct, and either to approve the fees or set the matter for further proceedings. ARIZ. R. OF CT. UNIFORM RULES OF PRACTICE FOR MEDICAL MALPRACTICE CASES Rule 3 (West 1997); see also *Ohliger v. Carondelet St. Mary's Hospital and Health Center*, 845 P.2d 523 (Ariz. Ct. App. 1992) (reversing trial court's approval, over malpractice plaintiffs' objection, of counsels' contractual fee of 40% of the recovery, and remanding for further proceedings).

51. See generally *Hoffert v. General Motors Corp.*, 656 F.2d 161 (5th Cir. 1981) (recognizing judge's power on own motion to reduce fee charged to minor in personal injury case).

52. See generally *McKenzie Constr., Inc. v. Maynard*, 758 F.2d 97 (3rd Cir. 1985) (enforcing contingent fee contract but recognizing that not all such agreements are enforceable on the same basis as other commercial transactions); *Anderson v. Kenelly*, 547 P.2d 260 (Colo. Ct. App. 1975) (affirming judgment that reduced contractual contingent fee that, in hindsight, seemed unreasonably large because the case turned out to be simple).

53. Resnik et al., *supra* note 20, at 325. The lawyers who are emerging as "tort class action" specialists enter litigation planning on its aggregation and hoping to be appointed to leading roles. *Id.* at 313. They think of themselves as financiers of a potentially massive economic deal. *Id.*

54. *Id.* at 394 & n.405 (stating that when individual claims are later transformed into aggregate litigation, judges sometimes "calculate the total attorneys' fees to be paid as the sum of all the individual contingency fee contracts entered into or that would have been entered into had each plaintiff [originally] retained his or her own attorney"). Such cases set non-contractual fee awards by reference to contingent fee contracts, rather than by external criteria. See, e.g., *In re Thirteen Appeals Arising out of the San Juan DuPont Plaza Hotel Fire Litig.*, 56 F.3d 295, 312 (1st Cir. 1995). There, 270 individual cases arising from a fire were filed in various courts, and then consolidated. *Id.* at 300. Once, consolidated, all the cases were managed largely by a subset of individually retained lawyers ("IRPAs"), whom the presiding judge appointed as the plain-

fees were constrained by new fee caps or other restrictions, judicial fee awards would presumably shrink as well. The individually retained lawyers and the appointed lawyers who manage the aggregate litigation could both lose and might, therefore, join together to oppose such constraints.

II. CONTINGENT FEE PROBLEMS WITH MANAGEABLE REGULATORY SOLUTIONS

One cannot usefully assess the value of contingent fee regulation without categorizing contingent fee problems or types of abuse, identifying various techniques for regulating contingent fees, and evaluating each technique as a response to specific problem categories. Broadly speaking, the problems that have troubled the contingent fee's critics over the years fall into four categories. Excessive fees, the problem category of central concern in recent years, will be the focus of Part III. The others, discussed here, include client confusion about the meaning and operation of contingent fee contracts, opportunistic use of contingent fee agreements to discourage clients from changing counsel, and perverse effects on lawyers' incentives in selecting and handling cases. Each discussion defines the problem, identifies regulatory responses to it, and evaluates the responses largely in terms of their administrability and legal-process costs. I conclude that regulatory techniques have been found that can control these problems at acceptable cost.

A. *Client Confusion About the Mechanics of Computing Contingent Fees*

When unsophisticated clients retain lawyers on a conventional hourly basis, perhaps to represent them in a divorce, they may have no clear idea how large the fee will ultimately be, but they will understand how it is to be computed. Such clients are less apt to understand the computation of a percentage contingent fee. Without regulation, contingent fee lawyers in the personal injury field could all too easily exploit their clients' naiveté about computation issues. This concern

tiffs' steering committee ("PSCs"). *Id.* When the cases settled, the judge determined what portion of the aggregate settlement to award as attorneys' fees by computing "the payments due under the various contingent fee agreements." *Id.* Interestingly, most of the original contingent fee contracts were capped under local law at 25% for minor clients or incompetents and one-third for adults. *In re Nineteen Appeals Arising out of the San Juan DuPont Plaza Hotel Fire Litig.*, 982 F.2d 603, 606 (1st Cir. 1992). The issue in the case was how the court should divide the overall fee award between the IRPAs and the PSCs. *Id.*; see generally Resnik et al., *supra* note 20 (discussing the complexities of dividing a fee award between IRPAs and PSCs and noting how little attention the issue has received).

has prompted regulatory responses of two kinds: formal contract requirements and the judicial construction of ambiguous contract terms against the lawyers who draft them.⁵⁵

A classic source of confusion involves the expenses, often substantial, that a contingent fee lawyer incurs in pursuing a case. Once a recovery is obtained, the lawyer will prefer to calculate the fee on the gross recovery, but the client will get a larger share if the fee is based on the net recovery after expenses are deducted. The problem is that in hiring the lawyer, if the retainer agreement was silent on the point, the client might have been oblivious to the issue or might have assumed without discussion that the net-recovery method would be used. No public policy dictates that fees be computed one way or the other,⁵⁶ but neither should the lawyer be permitted to exploit the client's *ex ante* ignorance by later applying the gross-recovery method and insisting, if the client questions the fee, that "that's how things are done." Accordingly, contingent fee contracts must now comply with formalities that counter this foreseeable source of confusion. Modern ethics rules, drafted by the ABA and adopted by the courts, require contingent fee agreements (but not other fee agreements) to be written, to state how the fee will be computed, and in particular, to indicate whether a percentage fee will be based on the gross or the net recovery.⁵⁷ In the event of a recovery, a lawyer must also give the client a closing statement showing how the fee was computed,⁵⁸ which the client can check against the written contract terms.

More generally, whenever a contingent fee contract with an unsophisticated client contains surprising or ambiguous computation provisions, and the lawyer tries to apply them in her favor, the courts will, at the client's urging, reject the lawyer's interpretation.⁵⁹ For exam-

55. See *infra* text accompanying notes 56-62.

56. The net-recovery approach might motivate the lawyer to economize on the expenses that are advanced, but this will not redound to the client's benefit if it encourages the lawyer to spend too little. Nevertheless, judicial rules in a few states require percentage contingent fees to be calculated on net recoveries. KANSAS RULES OF PROFESSIONAL CONDUCT Rule 1.5(d); N.J. R. OF CT. PRACTICE OF LAW AND ADMISSION TO PRACTICE Rule 1:21-7 (West 1997).

57. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5 (1994) (requiring contingent fee agreements to be in writing and to state, among other things, "whether such expenses are to be deducted before or after the contingent fee is calculated").

58. *Id.* Occasionally, special rules of court require closing statements to be filed with the presiding judge as well as the client. See, e.g., ARIZ. R. OF CT. UNIFORM RULES OF PRACTICE FOR MEDICAL MALPRACTICE CASE Rule 3 (West 1997).

59. Usually, the interpretation is rejected in a contract dispute. But, in an egregious case, a lawyer might also be disciplined for not stating the computation method clearly enough to satisfy the formal requirements of Model Rule 1.5(c). In *In re Struthers*, 877 P.2d 789 (Ariz. 1994), clients hired respondent to collect child-support arrearages for a 25% contingent fee. *Id.* at 791. Many arrearages were never collected in full, and few were collected in one lump sum. *Id.*

ple, consider the judicial response to the potential fee abuses associated with the modern development of structured settlements to resolve serious personal injury cases. Structured as opposed to lump-sum settlements provide periodic payments as the plaintiff's damages accrue over time.⁶⁰ They complicate the computation of percentage contingent fees in two ways. First, they make the value of the recovery on which the fee is calculated problematic. Suppose lawyer L negotiates and client C accepts a settlement calling for an immediate payment of \$100,000 plus annual payments of \$10,000 for the next ten years. Further suppose their contract states that in the event of a structured settlement, L's entire fee is to come out of initial payments, but leaves unclear how the settlement should be valued in order to compute the fee. If L proposes to value the settlement at \$200,000 and, therefore, to keep two-thirds of the initial \$100,000 payment, C might be too unsophisticated to question L's valuation. Courts have found it easy enough to minimize this problem by requiring lawyers in L's position to reduce the structured settlement to present value for fee purposes.⁶¹

Second, suppose a percentage contingent fee contract leaves unclear whether, in the event of a structured settlement, the fee will come out of the initial recovery or must instead be deducted from payments as received. The client might prefer the lawyer to take a percentage out of each payment as it is received; the lawyer might insist upon, and claim to have expected, full payment out of the initial recovery. In the 1980s, a handful of cases construing fee contracts that were silent or ambiguous on this point nipped the problem in the bud by invoking the familiar doctrine that ambiguous contracts should be construed against the parties who drafted them.⁶² It is now under-

Construing his fee agreements to entitle him to 25% of the *total* arrearage in each case in which *any* sum was collected, a reading supported by some terms but inconsistent with others, the lawyer treated all payments up to 25% of a total arrearage as his fee. *Id.* He sent no portion of those payments to his clients and never told them he had received the money. *Id.* The court found that the contracts did not state the fee computation method clearly enough to comply with ethical requirements. *Id.* at 795-96. For this and other misconduct, the lawyer was disbarred. *Id.* at 799.

60. WOLFRAM, *supra* note 6, at 533.

61. In Florida, lawyers must rely on the cost of any annuity the defendant purchases to fund the settlement or must reduce to present value all future payments to the client. FLORIDA RULES OF PROFESSIONAL CONDUCT Rule 4-1.5(f)(4)(B)(iii) (West 1997); see generally Doyle C. Valley, *Timing Payments of Attorney's Fees in Structured Settlements: Avoiding Problems with the "When Received" Approach*, 24 WILLAMETTE L. REV. 993 (1988) (discussing various approaches used by courts to value structured settlements for fee-computation purposes).

62. E.g., *Wyatt v. United States*, 783 F.2d 45, 50 (6th Cir. 1986); *In re Chow*, 656 P.2d 105, 113 (Haw. Ct. App. 1982); *Cardenas v. Ramsey County*, 322 N.W.2d 191, 193 (Minn. 1982). The cases also suggest that if the fee would consume a disproportionate amount of the initial lump-

stood that lawyers who expect to take their whole fee from initial payments must make that clear in their retainer agreements.

It would be naive to think that requiring contingent fee contracts to comply with certain formalities and construing ambiguous contracts against the lawyers who draft them prevent lawyers from ever exploiting client ignorance or confusion about fee-computation issues. However, these modest responses surely have some preventive effect, and achieve that effect without appreciably complicating the fee-negotiation process. More importantly for present purposes, they make no undue demands on the legal process. On the contrary, they forestall fee disputes that might otherwise have to be arbitrated or adjudicated; they require little enforcement effort;⁶³ and they are easily applied when they come into play in a legal proceeding. They simply put contingent fee lawyers on notice that fee-computation terms which are avoidably ambiguous or ignore simple formalities might not be enforced as the attorneys would wish and could even expose them to discipline. Lawyers can readily understand both the degree of clarity that regulators expect and the consequences of violating those expectations.

B. Lawyer Opportunism: Using Contingent Fees to Hold Clients Hostage

Because confidence in one's lawyer can be crucial to effective representation, many courts recognize a client's right to discharge a privately retained lawyer without incurring traditional contractual liabilities,⁶⁴ even when the lawyer has breached no contractual duties. Otherwise, lawyers could use certain fee arrangements to lock clients into relationships that become unsatisfactory. Conventional hourly

sum recovery, the lawyer should collect his fee on each payment as it accrues, whatever the contract may have provided. WOLFRAM, *supra* note 6, at 534.

63. Besides the occasional disciplining of lawyers who fail to comply with the contract formalities required by ethics rules, see *supra* note 59, courts may, in adjudicating a fee dispute, deny a non-conforming lawyer some or all of her contractual fee. See *Frank v. Peckich*, 391 A.2d 624, 638 (Pa. 1978) (affirming award of full fee under oral contingent fee contract, but only by an equally divided court, where ethics rule requiring a writing was not yet in force). On the use of fee forfeiture to sanction lawyers who violate ethical duties to clients, see *RESTATEMENT OF THE LAW GOVERNING LAWYERS* § 49 (Proposed Final Draft 1996).

64. See, e.g., *Salem Realty Co. v. Matera*, 410 N.E.2d 716, 719 (Mass. App. Ct. 1980), *aff'd*, 426 N.E.2d 1160 (Mass. 1981) (stating that "contractual yoking of lawyer and client" would undermine confidence in lawyers); *Plaza Shoe Store, Inc. v. Hermel, Inc.*, 636 S.W.2d 53, 58 (Mo. 1982) (en banc) (explaining why it is appropriate to confer this right on lawyers' clients but not on parties to other service contracts); *Martin v. Camp*, 114 N.E. 46, 48 (N.Y. 1916) (holding that a client may discharge his lawyer at any time without cause and without penalty). The client's right is sometimes known as the "client discharge rule." Lester Brickman, *Setting the Fee When the Client Discharges a Contingent Fee Attorney*, 41 EMORY L.J. 367, 367 (1992).

fees do not pose this problem. If L takes C's divorce case on an hourly-fee basis and the relationship sours, C can simply dismiss L, pay for the time L has already put in, and transfer the case file to successor counsel.⁶⁵ But suppose C agrees instead to pay L a \$2,000 non-refundable retainer, as well as an hourly rate of \$200. Weeks later, having paid the retainer, but not for the five hours L has so far devoted to the case, C decides that L is not the lawyer for him. Yet C finds it impractical to replace L unless L returns half the retainer, keeping the other \$1,000 as compensation for L's time. If L can keep the entire \$2,000 on the ground that it was no mere advance against hourly fees, C might find it easier to divorce his wife than his lawyer. To prevent lawyers from using non-refundable retainers to hold their clients hostage, several courts have recently declared them impermissible.⁶⁶

Contingent fees have a similar lock-in potential, but they are far too useful and widespread to ban on that ground. Suppose C retains L on a one-third contingent fee to pursue C's personal injury claim. L does some preliminary work, which C finds very disappointing but which involves no demonstrable breach of L's duties to C. C would like to discharge L in favor of lawyer M, who would also take the case on a one-third contingency. If discharging L in favor of M without legal cause would make C liable to each lawyer for one-third of any ultimate recovery, as general contract law would dictate,⁶⁷ then C would probably be deterred from making the change.

Many courts have responded to this potential lock-in effect by developing specialized doctrines for enforcing contingent fee agreements. Invoking the client-discharge principle, they deny the original lawyer a contractual percentage of the client's recovery and limit the lawyer to a quantum meruit award for pre-discharge work.⁶⁸ Because the award will often be lower than the contract fee, this approach

65. Of course, the client may incur expenses in finding a replacement and the new lawyer may have to duplicate some of the earlier work in order to get up to speed on the matter.

66. See *In re Cooperman*, 633 N.E.2d 1069, 1074 (N.Y. 1994) (banning non-refundable retainers). Since *Cooperman* was decided, many states have followed suit. Lester Brickman & Lawrence A. Cunningham, *Nonrefundable Retainers: A Response to Critics of the Absolute Ban*, 64 U. CIN. L. REV. 11, 11 n.2 (1995) (citing cases and ethics opinions). Where banned, non-refundable retainers become unethical, making their use a disciplinable offense, as well as unenforceable. The bans apply only to retainers that constitute fees for specific services, not to general retainers that pay lawyers for making themselves available to provide future services if and when the client needs them.

67. Brickman, *supra* note 64, at 371-72.

68. *Id.* at 373-74 n.37 (citing cases). A few states, including Texas, continue to allow the discharged lawyer to recover full contractual damages if the client later recovers on his underlying claim. *Id.* at 372-73 n.31.

tends to reduce the burden of changing counsel, yet leaves the original lawyer with some prospect of being compensated for the time devoted to the case. Of course, from a legal-process standpoint, this solution to the lock-in problem is not cost free. Adjudicating quantum meruit awards can be time consuming with outcomes difficult to predict.⁶⁹ Moreover, the solution raises new legal questions, such as whether the contract fee should operate as a cap on quantum meruit awards,⁷⁰ whether the original lawyer is entitled to quantum meruit even where the client has not yet achieved or never achieves a recovery,⁷¹ and how to discourage clients from exploiting the situation by discharging or threatening to discharge counsel on the eve of a settlement in order to avoid contractual fees or negotiate last minute fee reductions.⁷² These complexities notwithstanding, it is rare enough for contingent fee clients to change counsel in midstream that the legal-process costs of the quantum meruit response to the lock-in problem seem minimal. No evidence suggests that post-contract lawyer shopping and fee litigation are more common in states using the approach.⁷³

C. *Perverse Effects on How Lawyers Select and Handle Their Cases*

All fee arrangements have some potential to adversely affect the way lawyers select or handle their cases. For example, lawyers who are paid on an hourly basis but have less than a full caseload may be tempted to "run the meter"—i.e., devote more hours to a matter than is justified by their expected value to clients. Contingent fees may also have undesirable effects on case selection and management. Two different kinds of effects are conceivable. First, contingency fees may harm non-clients. By relieving clients of any duty to pay fees if their cases fail, contingent fee contracts could encourage frivolous suits, with resulting harm to the legitimate interests of adverse parties and

69. In adjudicating lawyers' quantum meruit claims, the courts rely heavily on factors identified in legal ethics codes as relevant to determine the reasonableness of a fee. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(a) (1994); MODEL RULES OF PROFESSIONAL RESPONSIBILITY DR 2-106(B) (1980). Applying those factors depends heavily on the facts of the particular case. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(a); MODEL RULES OF PROFESSIONAL RESPONSIBILITY DR 2-106(B).

70. See Brickman, *supra* note 64, at 380-81.

71. *Id.* at 381-85.

72. The few cases addressing this issue have found a "courthouse steps" exception to the quantum meruit approach, so that the discharged lawyer may well be entitled to her full contract fee if she can show that she was discharged on the eve of a successful recovery. See, e.g., *Fracasse v. Brent*, 494 P.2d 9, 14 (Cal. 1972); *McAvoy v. Schramme*, 189 N.E. 691, 691 (N.Y. 1933).

73. See *Sohn v. Brockington*, 371 So. 2d 1089, 1093 (Fla. Dist. Ct. App. 1979) (rejecting argument that the quantum meruit approach would produce "wholesale discharge of attorneys by clients shopping for the least expensive fees").

the courts themselves. Moreover, even in non-frivolous suits, contingent fee contracts could encourage lawyers to use unlawful tactics, such as introducing false evidence or lying about the extent of the client's injuries in settlement talks, in hopes of achieving the successful outcomes on which their fees depend.⁷⁴ In economic terms, these are externality problems⁷⁵ in the sense that the fee-induced misconduct infringes on the rights of third parties outside the attorney-client relationship.

Second, percentage contingent fee contracts create risks that lawyers will handle their cases in ways that disserve their clients. Since these fees do not compensate lawyers directly for their time, they could motivate lawyers to invest too little time in pursuing a case and to provide unreliable advice on the merits of a settlement offer. For instance, if L works on a unitary percentage contingent fee basis, L may prefer to settle early rather than risk spending additional hours to produce what L expects will be at best a minimally higher recovery and an insufficiently heightened fee to compensate for the extra time. Since those extra hours would cost C nothing, C may be disposed to reject the settlement. But C will probably rely heavily on L's advice about the desirability of the settlement, and that advice may be colored by L's personal interest in C's accepting the offer.⁷⁶ Settlement advice aside, L may be reluctant to spend any time preparing a case that cannot be justified by its expected return, even if it is likely to increase C's recovery somewhat. These biases pose agency rather than externality problems in the sense that they stem from fee-induced conflicts between the interests of client as principal and lawyer as agent.

1. *Externality Problems*

The argument that contingent fees encourage frivolous claims by freeing clients of all fee obligations when a case fails begins to seem frivolous itself when one considers the incentives the fees create for lawyers. Since the lawyers will only be paid if they achieve recoveries, they will generally have stronger incentives than hourly-rate lawyers

74. Clermont & Currivan, *supra* note 30, at 570-71.

75. See David B. Wilkins, *Who Should Regulate Lawyers?*, 105 HARV. L. REV. 801, 819-20 (1992) (distinguishing between lawyer misconduct that tends to harm clients, which Wilkins calls an "agency" problem, and misconduct harmful to others, which poses an "externality" problem).

76. In his empirical study of personal injury lawyers in New York City, Douglas Rosenthal found that they sometimes understate the amount of a defendant's proposal in discussing settlement offers with their clients, so that when clients are later told the correct amount of the offer, they will tend to accept it. DOUGLAS ROSENTHAL, *LAWYER AND CLIENT: WHO'S IN CHARGE?* 110-11 (1974).

to reject weak cases.⁷⁷ Moreover, they will usually be in a better position than their clients to judge a case's potential merit.⁷⁸ Still, a legally frivolous case is not inevitably unproductive from a contingent fee lawyer's standpoint. If the potential damages are huge in comparison to the time the case will require, or the defendant is likely to suffer substantial reputational damage by defending the case, or the case could conceivably smooth the way for future suits against the defendant by establishing a new precedent or uncovering damaging documents, then even an extremely weak liability claim may have considerable nuisance value. Since some medical malpractice or product liability cases that could not be pursued in the absence of a contingent fee arrangement do meet these conditions,⁷⁹ one cannot rule out the possibility that unregulated contingent fees promote frivolous claims in those fields.

One may, therefore, view the enactment in some states⁸⁰ of declining-rate contingent fee caps for plaintiffs' lawyers in medical malpractice cases as a regulatory response to the frivolous litigation concern.⁸¹ For example, California caps contingent fees for plaintiffs' lawyers in medical malpractice cases at forty percent of the first \$50,000 recovered, one-third of the next \$50,000, twenty-five percent of the next \$500,000, and fifteen percent of any additional recovery.⁸² By sharply

77. For a summary of empirical evidence supporting the view that contingent fee lawyers play a significant role in screening unmeritorious cases out of the civil justice system, see Herbert M. Kritzer, *Holding Back the Floodtide: The Role of Contingent Fee Lawyers*, WIS. LAW., Mar. 1997, at 10.

78. Clermont & Currivan, *supra* note 30, at 571; Stewart Jay, *The Dilemmas of Attorney Contingent Fees*, 2 GEO. J. LEGAL ETHICS 813, 814-15 (1989).

79. Suppose, for example, that C, who was badly injured in a car accident, proposes to retain L on a contingent fee to pursue a claim against the car manufacturer. Assume also that any case with no more than a 5% chance of producing a favorable judgment if litigated is frivolous. If L estimates that the likelihood of succeeding on the issue of liability is only 5%, but that C's damages would be assessed at \$1,000,000, she might place a \$50,000 value on the case (i.e., 5% of \$1,000,000). If L values her time at \$200 an hour and believes she will be able to extract a settlement of \$50,000 from the manufacturer after fewer than 100 hours of work, she might be willing to take the case for a 40% contingent fee. On a \$50,000 settlement achieved in 100 hours, she would receive a \$20,000 fee or \$200 per hour.

80. E.g., CAL. BUS. & PROF. CODE § 6146 (West 1993); 735 ILL. COMP. STAT. ANN. 5/2-1114 (West 1993); Richard M. Birnholz, Comment, *The Validity and Propriety of Contingent Fee Controls*, 37 UCLA L. REV. 949, 950-51 n.6 (1993) (citing comparable statutes from six other states).

81. See *Bernier v. Burris*, 497 N.E.2d 763, 779 (Ill. 1986) (upholding constitutionality of medical malpractice fee caps because the legislature could reasonably believe that the caps would "act as a disincentive for filing frivolous suits"); Patricia M. Danzon, *Contingent Fees for Personal Injury Litigation*, 14 BELL J. ECON. 213, 222 (1983) (inferring that avoidance of frivolous claims is the chief rationale for declining-rate contingent fee caps in medical malpractice cases). The American Medical Association supports such legislation. See AMERICAN MEDICAL ASSOCIATION, SPECIAL TASK FORCE ON PROFESSIONAL LIABILITY AND INSURANCE ACTION 6 (1985).

82. CAL. BUS. & PROF. CODE § 6146(a) (West 1993).

limiting the percentage fee a lawyer can earn in high damage cases, these caps could discourage lawyers from taking cases with very low odds that the defendant will be found liable, but with high potential damages if liability is found.

Of course, even if these caps do prevent some frivolous malpractice claims, they are an extremely blunt instrument for doing so, and may be undesirable as a matter of public policy. Declining-rate fee caps such as California's may also deter lawyers from accepting malpractice cases that are meritorious but will take great effort, especially if much of the effort would have to be channeled into extracting settlement concessions from the defendants for amounts over \$100,000.⁸³ Moreover, by restricting fees only in medical malpractice cases, such measures may also make it hard for severely injured malpractice victims to find effective representation. This is because personal injury lawyers, at least those most in demand, will tend to earn greater returns in uncapped automobile or product liability cases. And when lawyers do take malpractice cases, the caps may exacerbate agency problems by giving lawyers new incentives to underprepare or to talk their clients into accepting low settlement offers rather than shooting for higher awards from which the lawyer will get a decreasing marginal share.⁸⁴

These are valid objections to using declining-rate fee caps to deter frivolous claims. Notice, however, that they are not legal-process objections. Purely from the standpoint of minimizing the cost of judicial administration, using declining-rate fee caps to deter frivolous lawsuits, which are themselves a burden on judicial administration, seems unobjectionable. Fee caps are bright-line rules and essentially self-executing.⁸⁵ Lawyers will comply with fee caps, however grudgingly, knowing that non-complying fee agreements will not be enforced⁸⁶

83. Brickman, *supra* note 2, at 126; Danzon, *supra* note 81, at 30-31.

84. See Patricia Danzon, *An Economic Analysis of the Medical Malpractice System*, 1 BEHAV. SCI. & L. 39, 52-53 (1983). This problem can be mitigated but not avoided by treating the caps as presumptive rather than absolute ceilings, as is done in some jurisdictions. See *infra* note 85.

85. However, some states treat their contingent fee caps as presumptive rather than absolute ceilings and permit courts to make upward adjustments in some cases. See, e.g., FLORIDA RULES OF PROFESSIONAL CONDUCT Rule 4-1.5(f)(4)(B)(I) (West 1997) (setting fee caps for all personal injury cases and indicating that any fee in excess of the caps "shall be presumed, unless rebutted, to be clearly excessive"); *Id.* Rule 4-1.5(f)(4)(B)(ii) (permitting lawyer and client to petition trial court for relief from fee caps where the caps will otherwise block the client from obtaining the services of "an attorney of the client's choosing"). Treating fee caps as presumptions rather than absolute ceilings is unlikely to spawn fee litigation because few lawyers will contract for above-cap fees in hopes of overcoming the presumption once the case ends.

86. *Id.* Rule 4-1.5(d) (declaring lawyers' fee agreements that violate the contingent fee caps specified in the rule as unenforceable).

and could result in disciplinary sanctions.⁸⁷ Moreover, the caps will not spawn lawyer-client fee disputes because their application to specific cases is obvious.⁸⁸ They may even prevent disputes, since fees that do not exceed the caps are likely to be less susceptible to ex post attack as unreasonable than they would have been in the absence of the caps.⁸⁹

Unlike the concern about frivolous claims, no fee regulations have been proposed or enacted in response to the concern that contingent fees encourage lawyers to use improper tactics in achieving favorable results for their clients.⁹⁰ Instead, the matter is left to other laws, such as ethics rules and statutes forbidding the subornation of perjury,

87. See N.Y. R. OF CT. § 691.20(e)(1) (McKinney 1997) (indicating that a New York lawyer whose fees exceed statutory fee caps are subject to disciplinary sanctions).

88. In rare instances, however, a court may have to decide which of two facially relevant fee-cap statutes or rules governs the case at hand. See *Jackson v. United States*, 881 F.2d 707, 713 (9th Cir. 1989) (holding that the California medical malpractice fee cap is preempted by the higher federal cap on attorneys' fees in cases brought under the Federal Torts Claims Act); *Bernick v. Frost*, 510 A.2d 56, 61 (N.J. Super. Ct. App. Div. 1986) (holding that the New Jersey fee schedule governed permissibility of fee amount, rather than the more restrictive schedule of the state where litigation occurred, since the fee contract selected New Jersey law and most of the work was performed there).

89. See BRICKMAN ET AL., *supra* note 12, at 19 (criticizing contingent fee caps for failing to discriminate between cases which carry a high risk of failure and are likely to require great effort and cases where risk and effort are likely to be minimal). In California, for example, if L, working on a contractual contingent fee that called for the maximum percentages permitted under the caps, produced a settlement of \$50,000 for C, the court might allow her to collect a fee of \$20,000 (40% of the recovery), even if the case took only 10 hours of her time. In the absence of the caps, the trial court might at C's insistence be more disposed to reduce the fee, which amounts to \$2000 an hour, on the ground that it was "unconscionable" within the meaning of the state's legal ethics code. See, e.g., RULES OF PROFESSIONAL CONDUCT OF THE STATE BAR OF CALIFORNIA Rule 4-200 (West 1997) (prohibiting lawyers from charging "unconscionable" fees). Nothing in most fee-cap laws expressly precludes such review, and few cases address whether or not those laws take away judicial discretion, or relieve judges of any obligation, to review the reasonableness of a fee not exceeding the caps. But see 28 U.S.C. § 2682 (1982) (denying judge's discretion to reject as excessive any attorney's fee within the caps provided for claims under the Federal Tort Claims Act); *Jackson v. United States*, 881 F.2d 707, 713 (9th Cir. 1989) (holding that trial judge must accept a fee that was within the caps specified in 28 U.S.C. § 2682). What is clear is that trial judges do not relish the time-consuming task of reviewing lawyers' fees on a case-by-case basis and may welcome fee caps as an excuse for forgoing such reviews. Thus, in approving the Johns-Manville asbestos settlement, which imposed a 25% fee cap on lawyers who obtain awards for their clients from the settlement trust fund, Judge Weinstein treated those caps as a substitute for individual-fee review. See *In re Joint E. & S. Dist. Asbestos Litig.*, 878 F. Supp. 473, 557-58 (E. & S.D.N.Y. 1995) (acknowledging that the 25% cap would produce windfalls for lawyers in some cases, which could only be avoided by reviewing individual fees, but pointing out that the "transaction costs that would accompany consideration of fees for each claim" would be too great to justify the review), discussed in Susan P. Koniak & George M. Cohen, *Under Cloak of Settlement*, 82 VA. L. REV. 1051, 1099 n.163 (1996).

90. However, this appears to be one of several concerns that lie behind the ban on contingent fees in criminal defense work. See Karlan, *supra* note 7, at 610.

which govern all lawyers without regard to their fee arrangements.⁹¹ On reflection, this is not surprising. Other things being equal, the lawyer whose fee depends on a successful outcome might be more inclined to suborn perjury than the lawyer whose fee does not. But it is hard to imagine what restrictions on contingent fees, other than outright bans, could be fashioned to respond to the concern. Moreover, in personal injury litigation, other things are not equal. Corporate defendants and liability insurers, unlike personal injury plaintiffs, are repeat players in such litigation. There is no more reason to guard against overzealous conduct by plaintiffs' lawyers who work for contingent fees than to guard against such conduct by defense counsel who work for hourly fees (or as salaried employees of insurance companies), but hope their clients will be pleased enough with the outcomes of their cases to retain them again in the future.

2. Agency Problems

As noted, the chief agency problem posed by percentage contingent fees is the danger that lawyers will invest too little time to develop their cases fully enough to maximize their clients' net recovery.⁹² The danger results from the fact that percentage contingent fees reward lawyers for investing in their clients' cases but not directly for the time they invest. Again, no fee-regulation initiatives have been taken in response to this specific concern.⁹³ Some years ago, however, Kevin Clermont and John Currivan proposed such an initiative.⁹⁴ They would ban pure percentage contingent fees in favor of a more complex arrangement which they call the "contingent hourly-percentage"

91. Clermont & Currivan, *supra* note 30, at 570.

92. Of course, other agency problems could arise if lawyers were permitted not only to charge contingent fees but also to take by assignment an ownership interest in their clients' claims. That arrangement would elevate the lawyer from the status of agent to that of co-principal, and would invite the lawyer to make decisions, such as to reject a settlement offer or pursue an appeal, that may be contrary to the client's wishes and are normally decisions reserved for the client. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.2(a) (allocating decisionmaking authority between lawyer and client). Accordingly, the arrangement is banned. *Id.* Rule 1.8(j) (1994); see also *Goranson v. Solomonson*, 25 N.E.2d 930, 933 (Ill. App. Ct. 1940) (refusing to enforce an agreement assigning defense counsel an interest in some of the defendant's stock where the ownership of that stock was the very issue being litigated).

93. Of course, a personal injury lawyer who underworks can be liable to her client for professional negligence, but civil liability for negligence is not fee regulation. Moreover, where clients settle their underlying claims and later assert that but for the lawyer's negligent preparation or unreasonable advice the client would have recovered more, causation will be difficult to establish. At least one jurisdiction takes the extreme position that a lawyer cannot be liable to a client who agreed to settle his case except upon a showing of fraud. *Muhammad v. Strassburger, McKenna, Messer, Shilobod, & Gutnick*, 587 A.2d 1346, 1352 (Pa. 1991).

94. Clermont & Currivan, *supra* note 30, at 530-31.

fee.⁹⁵ Under their proposal, contractual contingent fees would have to be the sum of two factors: the lawyer's contractually negotiated time charge for the hours devoted to the case, capped by the amount of the recovery; and a modest percentage (set either by law or by contract) of the amount, if any, by which the client's recovery exceeds that time charge.⁹⁶ The percentage-of-recovery component would encourage the lawyer to economize on the time devoted to a case, as a pure hourly contingent fee would not.⁹⁷ But the time charge would assure that lawyers are compensated for each increment of time they devote to a case, thereby blunting their incentives to underprepare or to convince clients to accept unduly low settlement offers.

No jurisdiction has adopted this response to the primary agency problem associated with percentage contingent fees.⁹⁸ One explanation is that the proposal could generate some fees that eat up all or most of a client's recovery. Another is that it would require personal injury lawyers to maintain detailed time records, something they traditionally have had no need to do.⁹⁹ The proposal would also generate some, but presumably modest, administrative costs for enforcers. To deter contingent fee lawyers from charging personal injury clients for more hours than they actually work, trial courts and disciplinary agencies might have to review lawyers' time records in a significant number of cases. Yet, because most personal injury clients cannot or do not monitor their lawyers closely¹⁰⁰ and, therefore, would be unable to controvert a lawyer's time records, the reviews might ferret out few of the abuses that actually occur.¹⁰¹

95. *Id.* at 546.

96. *Id.* at 581-83. The lawyer's time charge in contingent fee cases will presumably be higher than her hourly rate in other matters, to allow for the risk that the cases will fail altogether or generate a recovery too low to compensate her for her time. *Id.*

97. *Id.* at 542-43.

98. One scholar has criticized the proposal as an inadequate response to the concern that lawyers are collecting excessive contingent fees, see Brickman, *supra* note 2, at 135, but that is clearly not the key concern that motivates the proposal. See Clermont & Currihan, *supra* note 30, at 534-37 (indicating that the agency or "conflict-of-interest" problem associated with percentage contingent fees is the chief concern).

99. Observers sometimes assert that plaintiffs' personal injury lawyers do not maintain contemporaneous time records for their personal injury cases. See, e.g., John F. Grady, *Some Ethical Questions About Percentage Fees*, 2 *LTIG.*, Summer 1976, at 20-21. But see Brickman, *supra* note 2, at 120-21 & n.365 (pointing out that lawyers whose contingent fees are set by courts in fee-shifting cases or in quantum meruit claims must present time records to justify their fees).

100. WOLFRAM, *supra* note 6, at 535 (suggesting that only sophisticated clients are in a position to monitor their lawyer's time commitments effectively).

101. See Jay, *supra* note 78, at 841 (suggesting reasons to doubt the reliability of personal injury lawyers' time records as a measure of professional effort). But see *id.* at 875 (suggesting that knowledgeable observers can detect time records that are false or padded with unproductive hours).

III. THE EXCESSIVENESS OF REGULATORY RESPONSES TO THE EXCESSIVE-FEE PROBLEM

As we have seen, courts, legislatures, and legal scholars have responded to some concerns traditionally associated with contingent fees by instituting or proposing regulatory measures that, whatever their merits in other respects, can be used effectively at acceptable administrative cost. Requiring contingent fee contracts to comply with certain formalities, and construing ambiguous contracts against the lawyers who draft them, help to prevent lawyers from exploiting client confusion about the mechanics of fee computation without making significant demands on courts or disciplinary agencies. Limiting contingent fee lawyers who are discharged without cause to quantum meruit awards for their time reduces the lock-in potential of contingent fee contracts without generating many additional fee disputes that must be adjudicated or arbitrated. Declining-rate fee caps in medical malpractice cases may reduce the incidence of frivolous claims without significant enforcement effort. In response to the agency problems associated with contingent fees, perhaps the courts could implement, at acceptable enforcement cost, the Clermont-Currihan proposal to ban pure percentage contingent fees in favor of contingent fees that combine hourly-rate and percentage-of-recovery features. But, when we turn to the chief concern of today's contingent fee critics, namely, that personal injury lawyers systematically reap windfall profits or excessive compensation via the contingent fee—the situation seems quite different. Regulatory measures taken or proposed in response to this concern either cannot be effectively administered or cannot be deployed at acceptable cost.

Much of the problem stems from the practical difficulty of constructing a reasonable fee baseline against which actual contingent fees can be judged for excessiveness. In theory, the optimal fee is the amount needed to induce a lawyer to take and properly handle a particular case. That amount is a function of the costs the lawyer expects to incur by taking the case. One of those costs is the lawyer's time and resources, which could be devoted to other work instead. The second cost is the risk the lawyer assumes that the case will produce no recovery or a recovery too low to generate a fee that compensates for the lawyer's time. If one could determine just how much risk of non-recovery a particular case posed when the lawyer accepted it, along with the size of the potential recovery, how much time the case would take, and the opportunity cost associated with the lawyer's time, then one could construct a baseline that would allow for reliable conclusions as to whether the lawyer's contingent fee was excessive—i.e., greater

than necessary to induce the lawyer to take the case and handle it properly. To take an oversimplified example, suppose that L takes divorce cases on a non-contingent hourly fee and personal injury cases on a percentage contingent fee. C hires L to represent him on a personal injury claim. Suppose L's non-contingent hourly fee is \$200, which by hypothesis is not excessive. Suppose also that in accepting C's case on a contingency, L knew the case would take exactly fifty hours and stood a fifty percent chance of achieving a \$100,000 recovery but an equal chance of achieving no recovery. If L produces a \$100,000 settlement after fifty hours and the contractual fee is twenty percent of the recovery, or \$20,000, one can say with confidence that the fee is reasonable. L will earn \$400 per hour, but will have assumed a fifty percent risk of earning \$0 per hour. Discounting the \$400 per hour by the fifty percent risk, one sees that L's "effective hourly rate"¹⁰² would again be \$200, which by hypothesis is not excessive.

In the real world, unfortunately, the information needed to construct such a baseline is rarely available. Lawyers may have no established hourly non-contingent fee or, if they do, the reasonableness of that fee may not be clear. More importantly, when lawyers and clients form relationships and agree on fees, the information available to the lawyers concerning the riskiness of the case, its time demands, and the potential recovery is often sketchy. And even if the information is extensive, no tribunal will find it easy, months or years later, to reconstruct that information for purposes of reviewing the reasonableness of the lawyer's fee. The question then, is this: What regulatory techniques, if any, can deal with these complexities at acceptable cost while reducing the incidence of excessive contingent fees?

A. *Case-by-Case Ex Post Review of Contingent Fees Under a "Reasonableness" Standard*

The oldest technique for protecting clients from excessive contractual contingent fees, and the technique least unacceptable to the plaintiffs' personal injury bar,¹⁰³ is to authorize a tribunal to review ex post the contractual fees earned in individual cases under a general standard of reasonableness. The review may be performed by the trial

102. Jay, *supra* note 78, at 840.

103. See, e.g., Philip H. Corboy, *Contingency Fees: The Individual's Key to the Courthouse Door*, 2 LITIG., Summer 1976, at 27 (arguing that availability of ex post review of reasonableness of contingent fees by disciplinary agencies obviates need for additional contingent fee regulation).

court in which the case was filed¹⁰⁴ or by a disciplinary agency¹⁰⁵ whose jurisdiction derives from the local adoption of ethics rules prohibiting lawyers from charging or collecting legal fees that are "unconscionable,"¹⁰⁶ "clearly excessive,"¹⁰⁷ or not "reasonable."¹⁰⁸ To convey a sense of the legal-process costs and other problems that stand in the way of ameliorating any truly pervasive problem of excessive contingent fees through case-by-case ex post fee review, I will focus on two cases from my home state of Arizona.

In *In re Swartz*,¹⁰⁹ the Arizona Supreme Court disciplined the respondent for charging a contingent fee that was "clearly excessive."¹¹⁰ After being badly injured in a job-related auto accident, the aggrieved client retained the respondent to represent him on a "third-party" personal injury claim against the responsible driver.¹¹¹ The fee was to be one-third of all sums recovered. Within two months and after minimal negotiations, the driver's liability insurers agreed to settle the matter for the full policy limits of \$150,000, thereby producing a \$50,000 payoff for the lawyer. The defense never disputed the liability issue; it soon became clear that the responsible driver had been intoxicated and no contributory negligence issue was raised. The insurers initially raised, but quickly dropped, a coverage issue.¹¹² Respondent never had to file a claim in the third-party action in order to obtain the settlement.¹¹³

104. See, e.g., *Anderson v. Kenelly*, 547 P.2d 260, 261 (Colo. Ct. App. 1975) (invoking the court's inherent power to regulate lawyers appearing before it as a basis for reducing a contingent fee that, in hindsight, seemed unreasonably large).

105. Though the disciplinary process in nearly every state is administered primarily by bar associations or by agencies under the supervision of the state supreme court, in cases where serious disciplinary sanctions are imposed, the respondent may petition the state supreme court for review. MODEL RULES FOR LAWYER DISCIPLINARY ENFORCEMENT Rule 31(B) (1993).

106. E.g., TEXAS RULES OF PROFESSIONAL CONDUCT Rule 1.04(a) (West 1997) (defining unconscionable fee as one that no "competent lawyer" would regard as "reasonable").

107. MODEL RULES OF PROFESSIONAL RESPONSIBILITY DR 2-106 (1980) (defining a clearly excessive fee as one that a lawyer of "ordinary prudence" would be firmly convinced was in excess of a reasonable fee, and listing among the factors relevant to such a determination: the time and labor required; the fee customarily charged in the locality for similar services; the lawyer's experience, reputation, and ability; and whether the fee is fixed or contingent).

108. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.5(a) (1994) (listing the same factors as relevant to a "reasonableness" determination as the Model Code lists as bearing on a determination of whether a fee is clearly excessive).

109. 686 P.2d 1236 (Ariz. 1984).

110. *Id.* at 1238.

111. *Id.*

112. *Id.* at 1239.

113. *Id.* This may explain why the excessiveness of the contingent fee came to be adjudicated in a disciplinary proceeding rather than before a trial court.

In the ensuing disciplinary proceeding, the State Bar disciplinary board found that respondent violated local ethics rules by charging a clearly excessive fee.¹¹⁴ On review, the court agreed. Though respondent testified that the settlement had taken a "tremendous amount of work,"¹¹⁵ he produced no time records to substantiate that claim and an expert witness called by bar counsel testified that respondent could not have spent more than twenty to thirty hours on the matter.¹¹⁶ Accepting the expert's testimony, the court found that the fee was excessive, suspended respondent's right to practice for six months, and ordered respondent to refund the excess portion of the fee (but without indicating how much of the fee was excessive).¹¹⁷

The court did not find that respondent's fee was excessive at the time respondent and his client agreed to it; indeed, it found to the contrary, implying that no rational *ex ante* baseline for judging the fee could be constructed, except perhaps by reference to the customary contingent fees charged in the respondent's community.¹¹⁸ Nor did the court assert that it was improper for the lawyer to reach a contingent fee agreement with the client before the lawyer could gain a full understanding of the case's potential.¹¹⁹ The point was, rather, that a contingent fee that is proper when contracted for may later turn out to be excessive. By the time of the settlement in this case it was obvious that the original fee was excessive, because the case proved to involve "no contingency, no difficult problem and little work."¹²⁰ The court held that, "[I]f at the conclusion of a lawyer's services it appears that a fee, which seemed reasonable when agreed upon, has become excessive, the attorney may not stand upon the contract; he must reduce the fee."¹²¹

One might infer that the court considered hindsight the ideal way to gauge the reasonableness of a contractual contingent fee, but this is doubtful. In theory, the inquiry ought to be whether the fee was sub-

114. *Id.* at 1238.

115. *Id.* at 1239.

116. *Id.*

117. *Id.* at 1248. Instead, the court suggested that if the lawyer and the client were unable to agree on a fee compromise the matter should be referred to the State Bar fee arbitration committee for resolution. *Id.* Suspension was considered an appropriate sanction because of certain aggravating factors not pertinent to the present discussion. *See id.*

118. *Id.* at 1243 (agreeing with respondent's contention that the one-third fee initially agreed upon was within customary limits for the type of case and was not excessive).

119. Notice that such a principle would not only undermine the view that lawyer and client should work out the terms of their fee agreement as early as possible, but would make it impossible for prospective clients to shop for lawyers on the basis of price before hiring one.

120. *Id.*

121. *Id.*

stantially in excess of the fee needed to induce the lawyer to take the case in the first place, an inquiry to which hindsight seems irrelevant.¹²² Moreover, a commitment to hindsight as the ideal perspective from which to gauge the reasonableness of a fee might suggest allowing *lawyers* to petition for higher-than-contractual fees if a case turns out to be more difficult or risky than lawyer and client could foresee when they agreed on a fee. Yet the court never hints that trial judges could or should entertain such petitions. In addition, the court's hindsight analysis may do very little to constrain the contingent fees that are charged to clients in the aggregate. Requiring lawyers to adjust contingent fees downward on the basis of hindsight, but never permitting upward adjustments in their favor, imposes on them the entire risk that *ex ante* fee agreements will be upset through *ex post* review. *Swartz* will, therefore, tempt lawyers to factor into their contractual fees a premium for running that risk. Clients such as *Swartz's* will then be protected from excessive fees at the expense of other clients who must pay that added premium, hardly a victory for clients as a class!

Swartz's insistence on the methodology of hindsight is better understood in legal-process terms. A tribunal reviewing the reasonableness of a contingent fee in hindsight can at least gather evidence on the amount recovered, the effort expended, and the difficulties the case ultimately presented. By contrast, deriving a baseline for judging the reasonableness of a fee by reconstructing what the lawyer knew or should have known when first taking the case will often be impossible, for the lawyer might have known, or may now claim to have known, very little indeed. One suspects, therefore, that the Arizona Supreme Court was drawn to the hindsight test not because it is theoretically the more valid measure of a fee's reasonableness, but as a concession to the impracticality of conducting an *ex post* review of the lawyer's *ex ante* information in order to construct a reasonable fee baseline.

Quite apart from the daunting methodological problems associated with *ex post* review of contingent fees under a reasonableness standard, the fact is that trial judges almost never initiate such reviews in the cases before them.¹²³ This too is understandable in legal-process terms. For one thing, without a client pressing the argument that a

122. See *Brobeck, Phleger & Harrison v. Telex Corp.*, 602 F.2d 866, 875 (9th Cir. 1979) (refusing to strike down on unconscionability grounds a lawyer's million dollar contingent fee from a sophisticated business client and noting that "whether a contract is fair or works an unconscionable hardship is determined with reference to the time the contract was made and cannot be resolved in hindsight").

123. For a rare instance in which an Arizona trial court, invoking *Swartz's* hindsight test, refused to enforce a plaintiffs' lawyer's contingent fee contract, see *In re Fallers*, 889 P.2d 20, 24

contingent fee is excessive, any court that initiates a review will lack the advantage of an adversarial presentation of evidence, which judges normally rely on to reach sound decisions.¹²⁴ Yet clients, with their recoveries fresh in hand, rarely see any basis for complaining that their lawyers' fee were excessive.¹²⁵ An even more fundamental problem is that judicial scrutiny of contractual contingent fees on any significant scale would make overwhelming demands on judicial resources.¹²⁶ Yet, if the excessive fee problem is pervasive and not just a matter of occasional overreaching, then rare instances of judicial review cannot be an effective response.

Of course, if the problem were simply that judges have strong motives not to review contractual contingent fees for reasonableness, one might argue that they should simply be ordered to do so. But the power of such mandates to stimulate careful review is doubtful. Since 1989, the Arizona Supreme Court has required the lawyers for all parties in medical malpractice litigation to submit a fee-and-expense statement to the trial judge after a settlement or verdict is reached. Within ten days of that filing, the court must either approve the fees as reasonable or set the matter for further proceedings.¹²⁷ Evidence suggests that some lawyers and judges are simply disregarding the mandate.¹²⁸ Since it became law, no reported cases have rejected a malpractice lawyer's fee as excessive.

This is not simply because malpractice plaintiffs and defendants fail to contest the reasonableness of the plaintiffs' lawyer's fee. In the one

(Ariz. Ct. App. 1994) (holding that the court was obliged to review fee agreement because plaintiff was a minor).

124. The lack of any devil's advocate to oppose the reasonableness of a fee is one reason why critics have serious reservations about the process by which judges review the fairness of class action settlements, including agreements on attorneys' fee awards. See, e.g., John C. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, LAW & CONTEMP. PROBS., Summer 1985, at 26-27; Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 45-47 (1991).

125. Lester Brickman, *A Massachusetts Debacle: Gagnon v. Shoblom*, 12 CARDOZO L. REV. 1417, 1428-29 nn.72-73 (1991).

126. See Brickman, *supra* note 3, at 1349-50 (estimating that one million new contingent fee cases are filed annually in American courts and pointing out that many other contingent fee representations involve matters never filed in court); cf. Charles Silver, *Unloading the Lodestar: Toward a New Fee Award Procedure*, 70 TEX. L. REV. 865, 906-07 (1992) (estimating that judicial fee setting under fee shifting statutes can take up to 10% of a federal judge's time).

127. ARIZ. R. OF CT. UNIFORM RULES OF PRACTICE FOR MEDICAL MALPRACTICE CASES Rule 3 (West 1997).

128. My colleague at the University of Arizona, Charles Ares, who has a longstanding interest in contingent fee regulation, recently told me that when he requested copies of the fee statements lawyers had filed under the uniform rules for malpractice cases, trial court clerks found no such documents on file. Interview with Professor Charles Ares, in Tucson, Ariz. (May, 1997).

reported case in which plaintiffs did dispute the reasonableness of the fee, the trial judge's fee review remained entirely pro forma. In *Ohliger v. Carondelet St. Mary's Hospital & Health Center*,¹²⁹ two lawyers represented a client on a medical malpractice claim after a sponge had been left in her body during an operation. The client and her lawyers entered into a forty percent contingent fee contract, but the lawyers assured her and her son, a New Jersey lawyer, that at the close of the case they would review the fee and revise it downward if it appeared excessive.¹³⁰ The case settled for \$550,000, earning the lawyers a contractual fee of \$220,000, or a bit over \$1,000 per hour, for a documented 213 hours of work. The lawyers considered the fee reasonable and the trial court reached the same conclusion, over plaintiff's objection, in its mandatory fee review.¹³¹ The client appealed. The appellate court reversed the order approving the \$220,000 fee and remanded for further proceedings.¹³² Noting that the mandate was silent as to the proper procedure for conducting a review,¹³³ the court analyzed the trial judge's review process this way:

We hold that when an objection is made to the fees, unless it appears as a matter of law that they are reasonable, the trial court must have an evidentiary hearing on the factors bearing on the reasonableness of the fee. . . . Because no such hearing was held in this case, we must remand for further proceedings. It is impossible sensibly to review the [trial judge's review of the] fee award when all we are confronted with is the argument on one side that \$1,000 an hour for a case where liability was clear is too high and the argument on the other side that 40% is the standard fee and in any event we did a terrific job.¹³⁴

Ohliger reveals the enormous difficulty of forcing trial judges to conduct the frequent and thorough ex post reasonableness reviews that might significantly affect contingent fee amounts. But even if those barriers could be overcome, the weaknesses of the hindsight test

129. 845 P.2d 523 (Ariz. Ct. App. 1992).

130. *Id.* at 524. Presumably, the lawyers had a duty to conduct such a review under the Arizona ethics rules as interpreted by the state supreme court in *Swartz*.

131. *Id.*

132. *Id.*

133. *Id.*

134. *Id.* Former Chief Judge Livermore of the Arizona Court of Appeals, who wrote the opinion in *Ohliger*, has told me in private conversation that, according to plaintiff's counsel, the trial judge on remand again approved the fee. Interview with Joseph Livermore, Former Chief Judge, Arizona Court of Appeals, in Tucson, Ariz. (May, 1997). Little evidence was introduced at the hearing. *Id.* The client simply introduced evidence that the fee would have exceeded the fee caps in effect in her son's home state, while the lawyers put in "expert" testimony from an insurance defense lawyer to the effect that the lawyers had achieved a good result in the case. *Id.*

and the lack of administrable alternatives leave it far from clear that closer and more frequent reviews would have desirable effects. To be sure, occasional decisions like *Swartz* may do no harm and they place no great burden on judicial resources. But they cannot be meaningful responses to the allegedly *pervasive* problem of excessive fees. It is hard to see how ex post judicial review under a general standard of reasonableness could be restructured to make that regulatory technique effective at acceptable cost.

All the barriers that stand in the way of effective but economical ex post fee review by trial judges apply as well to ex post review by disciplinary agencies.¹³⁵ Indeed, rare cases such as *Swartz* notwithstanding, a recent national survey of bar disciplinary counsel revealed that a client grievance about a disturbingly high contingent fee would probably trigger no disciplinary proceeding at all and would almost certainly not result in the imposition of discipline.¹³⁶ When the fee percentage is standard in the relevant community, disciplinary authorities will not examine the particular facts of the case to determine whether the fee was reasonable in the sense of being commensurate with the risk of non-recovery, the amount recovered, or the lawyer's time invested.¹³⁷ Many disciplinary counsel do not view fee disputes as raising ethical questions, but instead refer the aggrieved client to a fee-arbitration body.¹³⁸ They are obviously reluctant to spend their meager enforcement budgets on matters that do not involve stealing client funds or comparably serious offenses.¹³⁹ And, it is widely believed that a contingent fee excessive enough to warrant a trial judge's reducing it is not necessarily excessive enough to justify the imposition of professional discipline.¹⁴⁰

135. See Brickman, *supra* note 3, at 1356 (stating that case-by-case disciplinary enforcement fails for many of the same reasons that judicial enforcement fails).

136. *Id.* at 1359-73.

137. *Id.* at 1355.

138. *Id.*

139. In 1994, in New York City, for example, the local disciplinary agency's budget was only about \$35 per lawyer per year. Interview with Hal Lieberman, Chief Counsel, Departmental Disciplinary Committee of the New York Supreme Court, Appellate Division, in Naples, Fla. (May 27, 1994).

140. See RESTATEMENT OF THE LAW GOVERNING LAWYERS § 46 cmt. A (Proposed Final Draft 1996) ("In many jurisdictions, authorities have been reluctant to discipline lawyers [for charging unreasonably high fees]. For a variety of reasons, discipline might be withheld for charging a fee that would nevertheless be set aside as unreasonable in a [judicial] fee-dispute proceeding . . ."). Therefore, it is important to distinguish between applying reasonableness standards in fee disputes and in disciplinary proceedings.

B. Alternative Regulatory Responses

With the obvious failure of ex post review as a meaningful response to any pervasive problem of excessive contingent fees that may exist in the United States, a number of alternative regulatory responses have been proposed or adopted. Broadly speaking, these alternatives fall into two categories, which I shall call procedural and substantive responses. Procedural responses try to enrich the information available to a prospective client in deciding whether to accept the lawyer's proposed contingent fee agreement. Substantive responses restrict the permissible terms of contingent fee agreements. Neither category holds out much promise of constraining contingent fees at acceptable cost.

1. Procedural Responses

a. Mandatory Disclosures to the Client

One technique that might, in theory, reduce the incidence of excessive contingent fees would be to require lawyers to disclose information to prospective clients which would enable them to make better decisions as to whether to accept a proposed fee. If lawyers were compelled to give a prospective client some estimate of the odds of achieving a recovery, the expected amount of the potential recovery, and the amount of time the case will take, the theory goes, the client would be better able to choose between accepting the fee, negotiating for a reduction, or taking the matter elsewhere. Professor Lester Brickman once proposed, for example, that lawyers be required to use a standard contingent fee retainer form that would disclose the lawyer's estimates of these factors.¹⁴¹ The mandatory disclosures, he wrote, "will enhance the dormant competitive market forces operating on most contingent fee lawyers, while the forms will themselves exercise a regulatory function on attorneys, thereby diminishing the need for more intensive judicial scrutiny."¹⁴²

As a true regulatory requirement, however, rather than a mere aspiration for the plaintiffs' bar, this proposal has obvious drawbacks.¹⁴³ Initial estimates cannot be very accurate, given lawyers' unfamiliarity with most cases at intake. Estimating how long a case will take is inherently tricky because the lawyer's time investment will ultimately depend on how aggressively the case is defended, a matter outside the lawyer's control. Moreover, the lawyer will be tempted to offer esti-

141. Brickman, *supra* note 2, at 127.

142. *Id.*

143. ABA Comm. Ethics and Professional Responsibility, Formal Op. 94-389 (1994).

mates that are unreliable because they are calculated to convince the prospective client of the reasonableness of the proposed fee. The proposal would, therefore, have to be backed up by judges and disciplinary agencies scrutinizing estimates for deliberate misrepresentations. Yet, in the mine-run of contingent fee cases, it will be impossible to prove that the lawyer misrepresented her true estimates.

b. Mandatory Solicitation of Early Settlement Offers to Enhance Ex Ante Disclosures

Recently, Professor Brickman has acknowledged these drawbacks. In 1994, the ABA Committee on Ethics and Professional Responsibility ("CEPR") opined that, before finalizing a contingent fee agreement, the lawyer "should" generally discuss with a client the likelihood of achieving a recovery, the likely amount of the recovery, and the time the case is expected to take.¹⁴⁴ Brickman now derides this concession as "an unenforceable admonition,"¹⁴⁵ and not only because it stresses the word "should," rather than "must." The admonition would be unenforceable in any event, he admits, because a lawyer's "*failure to be candid would be virtually undetectable.*"¹⁴⁶

Recognizing that mandatory disclosure cannot in itself assure that clients get reliable information about the value of their cases before the fee is set, Brickman now argues that, contrary to CEPR's interpretation, the reasonable fee requirement of Model Rule 1.5 necessarily implies that:

[Contingent fee lawyers have] an ethical duty to seek out . . . settlement offers as soon as possible after entering into the attorney-client relationship in order to be able to disclose information to the client that will allow the client to give informed consent to the fee structure and in particular provide the client with a basis for determining whether it is beneficial to the client to agree to pay a standard contingency fee applied against the entire recovery.¹⁴⁷

In other words, Professor Brickman believes that the Model Rules should and do require contingent fee lawyers to solicit early offers and disclose them to their clients before the lawyers can reasonably contract for their standard contingent fee on the entire amount ultimately recovered. His reading of this strict protocol into Rule 1.5 is question-

144. See BRICKMAN ET AL., *supra* note 12, at 24-40 (presenting and defending the Manhattan Institute's "early offer" proposal)

145. See Brickman, *ABA Regulation*, *supra* note 12, at 294.

146. *Id.* (emphasis added).

147. *Id.* at 316 app. B (summarizing conclusions Professor Brickman believes CEPR should have reached, but did not, in Opinion 94-389).

able as a matter of policy and surely wrong as a matter of interpretation.

The policy rationale for a solicitation duty is that an early settlement offer, even if rejected, enables the client to gauge the lawyer's true risks in taking the case, because it establishes a minimum expected return—i.e., an amount as to which the risk of non-recovery is negligible.¹⁴⁸ Yet, a settlement offer that is rejected by the client and then withdrawn hardly assures that the offered amount will ultimately be recovered. It is *not* a reliable measure of risk for purposes of helping the client evaluate the lawyer's proposed contingent fee agreement.¹⁴⁹ Even if it were, the solicitation duty would not elicit this crucial information whenever potentially responsible parties chose not to make an early offer. Conversely, there are situations, such as airline crashes, in which potential defendants offer victims a settlement before counsel is retained.¹⁵⁰ In these situations, the prospective client can walk into a lawyer's office forearmed with a settlement offer, even though the lawyer has no duty to solicit an offer. Where there is no pre-retention offer, however, a duty to solicit offers before finalizing the contingent fee agreement could delay finalization for months.¹⁵¹ Most importantly, the solicitation duty that Brickman favors would intrude heavily on the autonomy of the lawyer-client relationship.¹⁵² Seeking an early offer has strategic implications for the

148. *Id.* at 332-33 (supporting solicitation duty to "ensure that clients and lawyers will not be obligated to speculate, at the client's disadvantage, about the risks or non-recovery that exist when they enter into contingency fee contracts").

149. See Susan P. Koniak, *Principled Opinions: Response to Brickman*, 65 *FORDHAM L. REV.* 337, 352 (1996) (arguing that an early settlement offer, once rejected, is "an unreliable indicator of how risky the suit may be to maintain").

150. After an airline crash, the airline's insurer:

usually sends out a letter admitting liability, indicating that . . . they will [soon] make a settlement offer and urging the victim or the family not to hire a lawyer until the offer is made. Once the offer is made, the claimants are urged and generally do go to lawyers and bargain for reduced contingency fees that in some cases only apply to the value the lawyer is able to add to the insurance company's offer.

Brickman, *ABA Regulation*, *supra* note 12, at 295-96.

151. With respect to how long Professor Brickman believes a lawyer and a client must wait for an early offer before finalizing their fee agreement, see *BRICKMAN ET AL.*, *supra* note 12, at 75 (proposing legislation or new judicial rules requiring early offer solicitation and requiring solicitations to include all "material facts relating to the claim," even where the claim is not yet filed and no discovery has begun). See also *id.* at 76 (proposing that allegedly responsible parties be given sixty days from receipt of a solicitation to decide whether to respond).

152. See Koniak, *supra* note 149, at 350-51.

To hold that lawyers working for contingent fees are ethically required to solicit early settlement offers, as Professor Brickman wanted [CEPR] to hold, would have . . . limited the kind of representation available to tort plaintiffs, because it would have dictated that their lawyers always adopt a particular strategy. Plaintiffs are not legally bound to solicit early settlement offers. To require their lawyers to do so is to require

lawyer's negotiations with potential defendants, not just for the lawyer-client relationship. Some clients may be disadvantaged by their lawyers soliciting an immediate settlement offer. Yet a rule obliging lawyers to solicit offers for fee-negotiation purposes could not be a mere default rule, waivable by the client's consent, because its whole purpose is paternalistic—to protect unsophisticated clients from over-reaching lawyers.¹⁵³

Whatever the policy merits of a duty to solicit early offers, Brickman's argument that CEPR should have found the duty implicit in Model Rule 1.5(a)'s terse requirement that legal fees be "reasonable" is clearly wrong. It disregards the legal-process constraints that CEPR faces as an interpretive rather than a legislative institution. Surely the ABA's legislative body, the House of Delegates, did not intend *sub silentio* to create a novel early offer solicitation duty for contingent fee lawyers, when in 1983 it adopted a general rule requiring all legal fees to be reasonable.¹⁵⁴ To find the duty implicit in Rule 1.5 would exceed CEPR's authority to render ethics opinions that *interpret* the Model Rules.¹⁵⁵ Moreover, even the House of Delegates would have good legal-process reasons not to amend the Model Rules to require early offer solicitation. The duty would be out of place in a legal ethics code which, as many commentators have noted, is designed to provide general ethical standards for law practice, not strict protocols or implementing regulations for lawyers specializing in a particular field.¹⁵⁶

all plaintiffs who hire lawyers on a contingency fee basis . . . to do so. I believe, however, that no reason exists to interpret (I would say stretch) the ethics rules to impose any such requirements on plaintiffs.

Id.

153. See Brickman, *ABA Regulation*, *supra* note 12, at 287-88 (explaining that plaintiffs must be bound by counsel's solicitation duty because that is the only way to protect them from over-reaching by contingent fee lawyers).

154. See, e.g., Ted Schneyer, *Professionalism as Bar Politics: The Making of the Model Rules of Professional Conduct*, 14 LAW & SOC. INQUIRY 677, 695, 736 (1989) (discussing sparse legislative history of the Model Rule 1.5 and finding no evidence that a contingent fee lawyer's duty to solicit early offers was considered in formulating the rule).

155. Although bar association ethics committees early in the century did not always treat their advisory opinions as exercises in ethics code interpretation, modern ethics opinions always purport to be interpretive. Ted Finman & Theodore Schneyer, *The Role of the Bar Association Ethics Opinions in Regulating Lawyer Conduct: A Critique of the Work of the ABA Committee on Ethics and Professional Responsibility*, 29 UCLA L. REV. 67, 69-70 n.4 (1981). Thus even a CEPR opinion that seems desirable as a matter of policy is open to criticism if it cannot be justified as an interpretation of existing Model Rules. *Id.* at 95 n.109.

156. See, e.g., Bruce A. Green, *Whose Rules of Professional Conduct Should Govern Lawyers in Federal Court and How Should the Rules Be Created?*, 64 GEO. WASH. L. REV. 460, 490 n.146 (1996) (quoting the ABA official view that the proper role of the Model Rules is "best served by preserving their character as relatively general statements of principle rather than detailed pro-

2. Substantive Responses

Two kinds of substantive alternatives to ex post reasonableness reviews have been put forth as desirable regulatory responses to the excessive fee problem. One approach is to ban or refuse to enforce "standard" contingent fee agreements when, or to the extent that, a client's case falls within an objectively defined category of cases that pose no genuine risk of non-recovery when the fee is set. The other is to adopt percentage fee caps as surrogates for the inherently vague "reasonableness" ceiling embodied in ethics rules.

a. Categorical and Partial Bans on "Standard" Contingent Fees

Lawyers occasionally try to charge hefty contingent fees (one-third or more of a recovery) for seeking to collect a client's property, no-fault automobile, or other first party insurance benefits.¹⁵⁷ When the insurer's obligation to pay is clear from the outset, no substantial risk of non-recovery exists. But the very attempt to charge a substantial contingent fee may lead a client to infer, mistakenly, that the matter poses such risk. Accordingly, ethics opinions have often found it improper for a lawyer to charge "substantial" contingent fees in such cases.¹⁵⁸ Courts have refused to enforce such fee arrangements,¹⁵⁹ and lawyers have occasionally been disciplined for using them.¹⁶⁰

Because engagements to collect first party insurance benefits are readily identifiable, a flat ban on contingent fees in such cases would be easy to administer. But no sensible rules on this subject can be so straightforward. Some first party insurance claims, such as those involving coverage disputes, carry serious non-recovery risks, so that a categorical ban on contingent fees in all first party insurance cases could limit access to representation for the claimants who need it most. Moreover, the relevant cases and ethics opinions do not bar contingent fees per se, only "substantial" contingent fees. This formulation is too unclear to prevent fee disputes—charging a fee of say,

scriptions for implementation of those principles"); Ted Schneyer, *From Self-Regulation to Bar Corporatism: What the S&L Crisis Means for the Regulation of Lawyers*, 35 S. TEX. L. REV. 639, 668-69 (1994) (explaining why the ABA cannot be expected to amend the Model Rules to include detailed protocols for performance of banking lawyer's work, even if such protocols might be desirable as a manner of policy in the wake of the savings and loan crisis); Fred C. Zacharias, *Specificity in Professional Responsibility Codes: Theory, Practice, and the Paradigm of Prosecutorial Ethics*, 69 NOTRE DAME L. REV. 223, 224-25 (1993) (stressing the limited extent to which an ethics code addressed to all lawyers can or should specify the conduct required in any specialty field, and suggesting that the Model Rules already approach the limit).

157. WOLFRAM, *supra* note 6, at 533.

158. Brickman, *ABA Regulation*, *supra* note 12, at 273 n.93 (citing numerous opinions).

159. WOLFRAM, *supra* note 6, at 533 n.51 (citing cases).

160. *Id.* at 553 n.52 (citing cases).

five percent of the proceeds on a property insurance claim might be reasonable given the time requirements of a case, while a twenty-five percent fee might not be. The "no-substantial-fee" principle therefore compels some case-by-case review to determine whether the contractual fee was proper.

In any event, the principle that "substantial" or "standard" contingent fees are improper in first party insurance recovery cases has no application to most personal injury cases, which seek compensation from liability, not first party, insurers. But it has inspired a broad proposal to bar personal injury lawyers from charging substantial or standard contingent fees against that portion of an eventual recovery which, by some objective measure, was never really at risk. This is the gist of the Manhattan Institute's recent call¹⁶¹ for legislation or judicial rules that require plaintiff's personal injury lawyers to solicit early settlement offers before they would be eligible to charge their standard contingent fees against any part of the ultimate recovery.¹⁶² Under this proposal, early offers would not serve merely as useful information for the client in negotiating a contingent fee. Rather, amounts offered as settlements before the lawyer is retained, or after retention but within sixty days of the lawyer's mandatory solicitation, would be deemed not to be at risk, and thus not subject to the standard fee, even when the offers are rejected and withdrawn.¹⁶³

This scheme would impose a substantial administrative burden on the injury victim's lawyer, because early offer solicitations must include "the material facts relevant to the claim," such as the basis for claiming that the solicited party is responsible for the client's injury.¹⁶⁴ Similarly, to ensure that claimants and their lawyers can meaningfully evaluate settlement offers, solicited parties who choose to make early offers must include any non-privileged materials relevant to the injury

161. BRICKMAN ET AL., *supra* note 12, at 69-83 (appendix presenting the proposal in statutory form).

162. *Id.* at 76 (proposed § 401(d) would allow a contingent fee lawyer who fails to solicit an early settlement offer to receive no fee greater than 10% of any recovery).

163. *Id.* at 76 (proposed §§ 601, 701-03, 801, explain the limited fees that can be charged against early offer settlement amounts, depending on whether the offers came pre- or post-retention, and whether they were accepted). For example, where post-retention early offers are rejected and the claims later produce a recovery, lawyers can only charge their standard percentage contingent fee against the amount of recovery in excess of the offered amount. As to the offered amount, lawyers are only entitled to an hourly fee for the time expended in generating the offer, but no greater than 10% of the first \$100,000 in the offer and 5% of any amount in the offer over \$100,000. *Id.* at 80-81 (§§ 701, 801).

164. *Id.* at 74-76 (§ 401, describing content of mandatory early offer solicitations).

which they “relied on” in developing their offers.¹⁶⁵ Thus, the proposal entails a discovery or disclosure process, even when a complaint has yet to be filed. To ensure that all relevant materials are disclosed, this process must be backed up by the threat of judicial sanctions for non-compliance,¹⁶⁶ thereby imposing new administrative burdens on the courts. Yet judicial enforcement of the offeror’s disclosure duties will be ineffective because it will rarely be demonstrable that the offeror failed to include all material “relied on” in developing its offer.¹⁶⁷

However administrable this scheme might be, its benefits to personal injury claimants are dubious. As noted earlier,¹⁶⁸ the duty of the claimant’s lawyer to solicit early offers is an intrusion on the autonomy of the lawyer-client relationship. In some cases, moreover, the scheme could result in claimants receiving larger *portions* of their recoveries, but smaller recoveries. Dooming plaintiff lawyers to considerably less than their standard percentages on any portion of an eventual recovery that was offered in an early settlement proposal, but was rejected, may aggravate the agency problem discussed earlier¹⁶⁹—plaintiff lawyers pressing their clients to accept settlement offers that do not maximize their net recoveries. Entitling lawyers to the standard one-third of the entire amount of any recoveries, if any, after settlement offers are refused, is more likely to make the lawyers’ settlement advice sound, than entitling lawyers to the standard fee only on the amounts by which the ultimate recoveries exceed the rejected offers. Recognizing this dynamic, potentially responsible parties under the early offer scheme may make more “low-ball” initial offers, some of which, regrettably, will be accepted.¹⁷⁰

Even putting these concerns aside, the early offer scheme may benefit some clients at the expense of others, yet afford personal injury

165. *Id.* at 77-78 (§ 502, describing material that must accompany early settlement offer in response to solcitation).

166. *Id.* (§ 401(e), providing for sanctions against non-complying contingent fee lawyers, and § 503, detailing legal consequences of a potentially responsible party’s failure to include prescribed material with the settlement offer).

167. *Id.* at 77 (§ 502).

168. See *supra* notes 152-53 and accompanying text.

169. See *supra* notes 76, 92-97 and accompanying text.

170. See Koniak, *supra* note 149, at 341. The proposal:

makes it much riskier [for the contingent fee lawyer] to fight through discovery and/or trial for a more just recovery for the client. The lawyer who fights might end up much poorer for his trouble than had he advised the client to take the low settlement without putting any energy in to the case. This is so because it is quite expensive for lawyers to fight. A client might have his recovery substantially improved by such a fight, but the lawyer would often be better off having moved on to the next settlement case . . .

Id.

clients as a class surprisingly little protection from excessive fees. If personal injury lawyers now charge their standard contingent fees against early offers, and if fee competition among those lawyers is as weak as proponents of the Manhattan Institute proposal insist,¹⁷¹ then nothing except fee caps—certainly not the hollow threat of ex post reasonableness review—would constrain lawyers from responding by *raising* their standard fees on recovery amounts above the early offer, or on entire recoveries where there is no early offer. In sum, although the Manhattan Institute's proposal is novel, even intriguing, there are good reasons to reject it.

b. Fee Caps

Finally, a number of states attempt to guard against excessive contingent fees by imposing flat or declining rate caps in tort, personal injury, or medical malpractice cases.¹⁷² Like the early offer proposal, fee caps undoubtedly avoid many of the legal-process restrictions and administrative costs that plague efforts to control fees through case-by-case ex post reasonableness reviews. The court or disciplinary agency that cannot decide swiftly and reliably whether a contractual fee is "reasonable" in hindsight can readily determine whether the same fee exceeds a crude one-third or forty percent fee cap. But the administrative savings associated with fee caps come at a heavy price and, in any event, should not be overestimated. Used as surrogates for a reasonableness standard, fee caps are inherently overbroad and underbroad, even if by some miracle they happen on average to provide the compensation needed to induce a lawyer to take meritorious cases and handle them properly. There will be serious injury cases where the risks of non-recovery are nonetheless substantial and enormous effort will be required in order to prevail. There will also be small damage cases in which lawyers foresee that they will require a fee above the caps in order to be compensated reasonably for their time.¹⁷³ If the fee caps are rigorously enforced, the effect in these cases could be to deny would-be clients access to representation.¹⁷⁴

Of course, one can try to manage this problem, as fee-cap jurisdictions often do, by treating the caps as "presumptions" and allowing

171. BRICKMAN ET AL., *supra* note 12, at 23 (ascribing the "increasingly greater returns available to plaintiffs' attorneys" to "the fact that most personal injury claimants seldom have more than one claim per lifetime and thus lack the experience or leverage to bargain down the *oligopsonistic* rates which their lawyers set") (emphasis added).

172. See *supra* notes 39, 80.

173. See BRICKMAN ET AL., *supra* note 12, at 19.

174. Clermont & Currivan, *supra* note 30, at 580-81 (stating that fee caps will likely result in some potential clients' inability to find lawyers who will even accept their cases).

lawyers and clients to petition judges for case-by-case exceptions.¹⁷⁵ But that procedure, if used frequently, reintroduces substantial administrative costs for the courts. At the same time, it frustrates the very purpose for which caps are imposed. Observers have found that “[c]ourts seem to grant exceptions . . . routinely on such justifications as the quality of the lawyer or the impressive size of the recovery, as if success in the representation had not already been worked into the formula.”¹⁷⁶ At the same time, where exceptions are not granted *ex ante* or cannot be expected *ex post*, the caps simply invite lawyers to underwork.¹⁷⁷ As Clermont and Currivan concluded twenty years ago, fee caps “are largely cosmetic, keeping the final fee at what seems a reasonable level to the outside observer, while still permitting the lawyer covertly to pick and then milk (through underwork) the lucrative cases.”¹⁷⁸

IV. CONCLUSION

Certain problems associated with the plaintiff lawyers’ use of contingent fees in personal injury cases have proven to be controllable at acceptable cost through regulation. These problems include client confusion about the mechanics of calculating contingent fees, the potential lock-in effect of contingent fees on clients, and some of the perverse effects contingent fees can have on a lawyer’s selection and handling of cases. The allegedly pervasive problem of excessive contingent fees, which for the sake of argument I have treated as a real problem, has proven more resistant to effective regulatory control through any method whose administrative and other costs are sustainable. Courts and disciplinary agencies are in no position to exert any real influence on contingent fee amounts through occasional *ex post* fee reviews under the reasonableness standard. If they began to review contingent fees more aggressively and frequently, they would have to devote enormous time to the task and would still be hampered by the lack of an appropriate baseline for judging reasonableness. Yet, fee caps and the early offer proposal, which rely on objective surrogates for the reasonableness standard in order to skirt these difficulties, are very crude alternatives—easier to administer, perhaps, but offering no real assurance of improving client welfare.

Despite its skepticism about the value of existing and proposed techniques for controlling contingent fee amounts through regulation,

175. See *supra* note 39.

176. WOLFRAM, *supra* note 6, at 535.

177. *Id.*

178. Clermont & Currivan, *supra* note 30, at 581.

this Article should not be read as a paean to the free market. In view of the attractiveness of the personal injury plaintiffs as candidates for regulatory protection, it is surely sensible for scholars and policy makers to continue to search for worthwhile fee control techniques. One can only hope, however, that the search will be guided by an appreciation of the institutional limits that constrain courts, legislatures, and the bar as designers and enforcers of fee regulations. Without that appreciation it is all too likely that additional contingent fee regulation will do more harm than good for injury victims, while making unrealistic demands on legal institutions.